VA INSURANCE PROGRAMS

HEARING

BEFORE THE

SUBCOMMITTEE ON
COMPENSATION, PENSION AND INSURANCE

OF THE

COMMITTEE ON VETERANS' AFFAIRS
HOUSE OF REPRESENTATIVES

ONE HUNDREDTH CONGRESS

FIRST SESSION

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VA INSURANCE PROGRAMS

Thursday, September 10, 1987

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMPENSATION, PENSION
AND INSURANCE,
COMMITTEE ON VETERANS' AFFAIRS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:08 a.m., in room 334, Cannon House Office Building, Hon. Douglas Applegate (chairman of the subcommittee) presiding.

Present: Representatives Applegate, Penny, Evans, McEwen and Bilirakis.

OPENING STATEMENT OF CHAIRMAN APPLEGATE

Mr. APPLEGATE. Good morning. I'm sorry for the delay, but there are other activities going on in the House of Representatives and I had to attend one of those other early morning meetings.

We are meeting this morning in an oversight hearing to get a report on the status of the various insurance programs of the Veterans' Administration. Today we will hear testimony from representatives of the VA, as well as the PVA and the VFW.

I would like to say that the insurance programs seem to be running rather smoothly. The number of inquiries or complaints from insured veterans about their insurance is very low compared with many of the other programs. This is a tribute to the Veterans' Administration officials who have managed this program over the years.

I especially want to compliment John Vogel on the prompt responses and compassionate service rendered recently to the survivors of active military personnel who lost their lives during incidents such as the missile strike on the *USS Stark,* the Gander plane crash, and the Beirut bombings. The actions of the VA, the Office of Servicemen's Group Life Insurance, and the Department of Defense in providing prompt casualty assistance are highly commendable, and the committee, John, is grateful to you and your staff.

Our first witness this morning is the VA's Chief Benefits Director, Mr. John Vogel. Of course, it is always a pleasure to welcome him to the committee. It seems to me that the first time John appeared before the subcommittee in his capacity as the Chief Benefits Director was 2 years ago, just about on this date, I think, and it was our last insurance oversight hearing. Prior to that time, he was the director of the insurance operation in Philadelphia and is certainly well-versed in that activity. Therefore, we on the commit-

tee are looking forward to hearing about the current condition of the programs and the actions that you have taken since we last met on this subject. I am glad to have you here today, along with Mr. Carey, Mr. Thompson, and Mr. Koons.

After we hear from the Veterans' Administration, we will also be hearing from Bob Moran from the PVA—Bob, it's always good to see you here—and Mr. Gordon Thorson of the VFW.

At this time I would like to recognize my very good friend and colleague, the vice-chairman of the subcommittee, Mr. McEwen.

OPENING STATEMENT OF HON BOB MCEWEN

Mr. MCEWEN. Thank you, Mr. Chairman.

This subcommittee, under your leadership, has kept a careful eye on the VA's life insurance programs, and I commend you for calling the hearing to continue the subcommittee's oversight. I hope that this oversight has, in part, contributed to the VA's excellent record in its life insurance programs, which have been effectively managed and almost trouble free.

There is an area in which we have had a minimum of constituent complaints. I am pleased that, according to Mr. Vogel's written statement, the one area which was producing some complaints, the interest rate on National Service Life Insurance policy loans, is being addressed by regulatory change.

These programs have been a good bargain for the taxpayer because of their very low cost, and they have been of great benefit to many veterans and their survivors.

Mr. Chairman, I support the VA's life insurance programs and the continuing efforts to make them even better. I look forward to hearing the testimony of Mr. Vogel, the VA's Chief Benefits Director, and I join you in welcoming him and the program managers who accompany him, Mr. Robert Carey and Mr. Paul Koons, Director and Assistant Director of VA's Philadelphia Insurance Center.

Thank you, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. McEwen.

Mr. Penny.

Mr. PENNY. Thank you, Mr. Chairman.

I, too, look forward to the testimony that will be presented at this morning's hearing. Particularly, I want to thank the VFW for a resolution they adopted at their recent convention endorsing the retention of the VA Regional Insurance Center at St. Paul, MN. This committee reported to the House floor and the House acted favorably on a bill that, among other things, would include the retention of the St. Paul center. I am curious this morning to hear from Mr. Vogel as to the Department's intentions, given the fact that that bill is moving along, and what their thoughts are on the consolidation issue.

With that, Mr. Chairman, I yield back my time.

Mr. APPLEGATE. Thank you, Mr. Penny.

Mr. Bilirakis.

OPENING STATEMENT OF HON. MICHAEL BILIRAKIS

Mr. BILIRAKIS. Thank you, Mr. Chairman.

Although, as you know, sir, I have been a member of the Veterans' Affairs Committee since coming to the Congress, this is my first year as a member of this subcommittee, so I especially appreciate hearings such as this which give me an opportunity to learn about the programs under our jurisdiction.

In reviewing Mr. Vogel's testimony, I was very impressed with his report on the financial soundness of the insurance programs administered and supervised by the VA, and with the timeliness of VA's responses to beneficiary claims and questions.

Too often we hear complaints from our constituents about long waits and slow response times for VA health care and home loans. While I understand that some delays are unavoidable, it is certainly nice to hear the good news about this program.

I am also anxious to hear from the VA on the feasibility of implementing improvements in these insurance programs as proposed by the PVA and the VFW. Ideally, we want these programs to more fully meet the needs of the veterans for whom they were created while remaining financially sound.

Mr. Chairman, with your permission, I would like to very briefly allude to the recent national convention of the Uniformed Services Disabled Retirees, which was held in Albuquerque, NM. I was asked to be a keynote speaker there. I would just again plead publicly to you, Mr. Chairman, that we hold hearings on bill H.R. 303, which basically eliminates the offset which requires, in essence, that the veteran pay out of his retirement pay, which he has earned, for his disability compensation, which he also has earned. I think it is significant enough, Mr. Chairman, with 103 cosponsors, including myself—and there may be more now—that we at least pull it out of the doldrums and talk about it somewhat here in our hearings and hopefully go forward with it.

Thank you very much, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. Bilirakis.

Mr. Evans?

Mr. EVANS. Thank you, Mr. Chairman. I have no opening statement.

Mr. APPLEGATE. Okay. I thank the gentlemen of the committee. Now we will hear from Mr. Vogel.

STATEMENT OF R. J. VOGEL, CHIEF BENEFITS DIRECTOR, VETERANS' ADMINISTRATON; ACCOMPANIED BY ROBERT CAREY, DIRECTOR, PHILADELPHIA REGIONAL OFFICE/INSURANCE CENTER; PAUL KOONS, ASSISTANT DIRECTOR FOR INSURANCE, PHILADELPHIA INSURANCE CENTER; AND JOHN H. THOMPSON, ASSISTANT GENERAL COUNSEL, OFFICE OF GENERAL COUNSEL, VETERANS' ADMINISTRATION

Mr. VOGEL. Thank you very much, Mr. Chairman.

I very much appreciate those gracious remarks you made about the management of the insurance programs. The people to whom we would like to pass that message on are the people at the Philadelphia and St. Paul Insurance Centers, who work so effectively and so compassionately in those programs. I will pass your remarks on and appreciate you making them, sir.

We appreciate the opportunity to address the subcommittee in reviewing the status of the insurance programs. Rather than reading the entire text of the testimony we have submitted for the record, I would like to focus my remarks today on the changes we have implemented since the last insurance oversight hearings. I would also like to outline our current initiatives designed to enhance program benefits and improve the administration of our programs.

One financial benefit enhancement which we were able to implement on January 1 of this year was a 15 percent increase in the face value of existing paid-up additional coverage. Along with this one-time increase in coverage, policyholders who elect to use their dividends to purchase paid-up additional coverage can now buy 15 percent more of this type of coverage with each dividend dollar.

Approximately 800,000 policyholders initially benefited from this increase. The total value of this one-time coverage increase was $350 million.

Another enhancement that is now in the final implementation stage is the change to a variable interest rate on the National Service Life Insurance policy loans. The initial rate will be set at 8 percent per annum and will be in effect at least through September, 1988. The rate will be adjusted based on the performance of an economic indicator, the indicator being the June interest rate on U.S. Treasury securities, 10-year constant maturities. We will monitor the indicator and adjust the rate whenever it rises above the next whole number or falls below the current rate.

For example, if the indicator rises to 9.2 percent in June of next year, the policy loan interest rate would be raised to 9 percent effective that October. On the other hand, if the indicator falls to 7.55 percent, the policy loan interest rate would be dropped to 7 percent. The variable interest rate will have a minimum floor of 5 percent and a maximum ceiling of 12 percent. Any change in the interest rate will take effect on October 1 of a given year.

We believe that a variable interest rate with the use of an economic indicator is a more equitable method of determining the policy loan interest rate because it allows the earnings on loans to be more in line with the earnings on other types of trust fund investments. As a result, policyholders with loans and those who have not borrowed on their policies are treated the same for dividend distribution purposes, since dividends for all policyholders are based, in part, on the investment earnings of the programs' reserves. We expect the new rate will take effect in late October of this year.

One of our current legislative initiatives is the proposal which has been included in H.R. 2008. This initiative would grant the Administrator the authority to periodically increase the amount of the monthly installment payments to beneficiaries who receive payments under an annuity option. If the proposal is enacted, we plan to increase the NSLI (V) policy annuity payments by 50 percent for the next 5 years.

We are able to recommend this action because of the high yields on reserves held for the payment of (V) annuity settlements. Future adjustments will depend on the reserves' interest earnings and the mortality experience of this group. Approximately 130,000

beneficiaries will benefit from this initial increase in annuity payments.

In addition to implementing the program enhancements I have just described, we are also making progress toward our goal of redesigning and upgrading the ADP system which supports the insurance program. Phase I, or the inquiry phase of our redesign project, was completed in 1985. The second phase, the data entry phase, is partially complete. Among the functions that can now be accomplished on line is the processing of policy loans and changes of address. On-line processing offers advantages such as the editing and correcting of transactions before they are submitted for processing. Because of this editing capability, we expect to make significant improvements in the quality and timeliness of our processing. We estimate that Phase II of that project will be completed in March of 1989.

An equally important aspect of the redesign project is the conversion of our data processing programs from an outdated programming language to a modern language. The conversion of the programs will enable us to make modifications to eliminate processing restrictions which now require a significant amount of clerical intervention. The conversion of the insurance programs is expected to be completed by the end of next year.

Shifting the focus to the insurance programs we supervise, I would like to briefly discuss the Servicemen's Group Life Insurance and Veterans Group Life Insurance programs.

Since our last oversight hearings, Public Law 99-166 went into effect on January 1, 1986, increasing the Servicemen's Group Life Insurance coverage from a maximum of $35,000 to a maximum of $50,000 for all individuals on active duty and members of the ready reserves. This change resulted in an automatic increase in coverage of over $52 billion.

Because of the favorable investment and claims experience in the SGLI program, we have been able to maintain the premium rate at a low cost of $4 per month for the maximum coverage of $50,000. The new law also extended VGLI coverage to members of the individual ready reserves and the inactive National Guard. Although we conducted a mailing to the 420,000 individuals in this reserve status, only 3.6 percent applied for the coverage.

One of our concerns in the VGLI program, which insures recently separated veterans, members of the individual ready reserve, and the inactive National Guard, has been the sharp decline in participation in recent years. Within the last 2 years we have taken several actions, in cooperation with the Office of Servicemen's Group Life Insurance, to reverse the trend.

We are testing an initiative which allows separating service members to enroll for VGLI when they separate and have the initial premium deducted from their final pay. We tested that at the Fort Dix separation center and it worked rather well. Some 70 percent of those offered the opportunity did apply for VGLI coverage. The Department of Defense has agreed to implement this enrollment process at major separation transfer points around the country.

We have also restructured VGLI premium rates from two age brackets to six. The rates in the new structure are designed to

cover the mortality expenses and administrative costs for each age group. The new rates were effective July 1, 1986, and represent a 30 percent reduction for 80 percent of those insured in the VGLI program.

We have begun to offer retirees the option of paying VGLI premiums by deduction from retired pay. Army and Air Force retirees can now participate, with the remaining services to follow shortly. We are also exploring the possibility of allowing a deduction of VGLI premiums from VA benefits. In addition, at our request, the Office of Servicemen's Group Life Insurance will begin offering a discounted annual premium payment option next month.

As a result of these actions, I am pleased to report that the participation rate in the VGLI program increased from 20 percent in policy year 1985 to 24 percent in policy year 1986. We expect to see it continue to rise as the new initiatives are implemented.

From a financial standpoint, all of the programs are in sound financial position. Two programs which require annual subsidies are the Service Disabled Veterans Insurance, the SDVI program, and the Veterans Mortgage Life Insurance, the VMLI program. The SDVI program required a subsidy of $7 million in fiscal 1986, and the VMLI program subsidy amounted to $4.4 million.

In the area of cash management, at the last oversight hearings we reported that we were acquiring new remittance processing equipment. It became operational in October of last year and we have been able to reduce the remittance processing staff by 35 percent and still meet our timeliness standards. We currently deposit 95 percent of our insurance premium payments on the same day they are received.

As part of our comprehensive cash management program, we developed a new premium option that will allow us to draft premium payments from policyholders' checking accounts through Treasury's electronic funds network. This initiative will not only reduce our processing float but will also provide policyholders with the additional flexibility of another premium payment option.

The total cost to administer the NSLI, VSLI, SDVI and USGLI programs last fiscal year was approximately $26 million. The average cost to maintain each policy in these programs was $6.97. Since the premiums paid by those insured under the SGLI and VGLI programs cover the administrative expenses as well as the normal mortality costs, there was no cost to the Government in administering those programs.

One final note before I conclude my remarks. There were two unfortunate military tragedies that you referred to, Mr. Chairman, that occurred since our last opportunity to present testimony—the Gander airline crash and the attack on the *USS Stark*. Between these two incidents, there were a total of 285 casualties. Only one of those individuals was not covered by SGLI insurance. We attribute that high coverage rate to the automatic coverage feature of the SGLI program. In each of these instances, the Office of Servicemen's Group Life Insurance implemented special procedures to expedite the payment of these claims. Policy proceeds were authorized no later than one day after all the necessary documentation was received.

Mr. Chairman, this concludes my prepared remarks. As requested, we have limited the length of our prepared testimony for the record to ten pages. However, we are prepared to submit a set of exhibits for the committee's files which include individual program summaries and program statistical data, as well as investment yield and investment portfolio information.

We would be pleased to answer any questions that you or any members of the subcommittee may have, Mr. Chairman.

[The prepared statement of Mr. Vogel appears at p. 21.]

Mr. APPLEGATE. Thank you very much, John. I appreciate your testimony, as always.

I understand that a GAO study recently advised that the Veterans' Administration was holding what they considered to be too much in reserves. Would you like to comment on that?

Mr. VOGEL. I would like Mr. Carey to respond to that, Mr. Chairman.

Mr. CAREY. Yes, sir. In conducting their analysis, GAO used what is referred to as "generally accepted accounting principles". The reserves for the insurance program, however, are based on what's called the "statutory accounting principles". These are the accounting principles that are used throughout the insurance industry and are used by almost all mutual companies in the country and are required by most States for those individual companies. So we feel, based on that fact, that the reserves that we keep are proper.

Mr. APPLEGATE. I imagine they're proper. I am wondering why they said that, but let me ask you this, do you have a copy of the report?

Mr. CAREY. Yes, sir.

Mr. APPLEGATE. And have you prepared a response?

Mr. VOGEL. We are going to respond and elaborate on the fact that we believe they have applied the wrong accounting principles. They applied principles that are really not applicable to mutual insurance operations, which is essentially the nature of the programs that we administer.

Mr. APPLEGATE. Yes. We would like to have a copy of the report and a copy of your response, if you would.

Mr. VOGEL. Yes, sir.

[The information follows:]

GENERAL ACCOUNTING OFFICE REPORT TO THE CONGRESS: VETERANS ADMINISTRATION'S FINANCIAL STATEMENTS FOR FISCAL YEAR 1986

The references to the insurance reserve balances are found in the last paragraph on page 6 of the report, and in Note 5 which is found on pages 22 and 23.

Although the VA was not asked to provide formal comments on this report, we were given the opportunity to make an informal response to their draft report. In our discussions with GAO, we pointed out that our actuaries use the Statutory Accounting Principles that are used throughout the life insurance industry by mutual life insurance companies. The use of these Statutory Accounting Principles is required by state government regulations and is endorsed by the National Association of Insurance Commissioners (NAIC) as well as the National Academy of Actuaries and the Society of Actuaries for the purpose of determining reserve level requirements for mutual life insurance companies. We also pointed out that if the VA were to reduce its reserves to the levels suggested by GAO that we would not be able to cover the policy reserves (cash values) that have accumulated on the permanent plans of insurance that we have issued. Over 71 percent (over $9.2 billion) of the reserves held by the VA represent policy reserves on permanent plans of insurance.

The Standard Valuation Law recommended by the NAIC states that "In no event shall a company's aggregate reserves for all life insurance policies...be less than the aggregate reserves calculated in accordance with the...mortality tables and rate of interest used in calculating non-forfeiture benefits for such policies." In the VA's case the policy reserves represent the "non-forfeiture benefits" referred to in the NAIC's Standard Valuation Model Law. As a result of our comments, the note (Note 5) on the Life Insurance Programs was modified to reflect the fact that, "The statutory accounting principles used by the VA are the same as those used by many mutual life insurance companies in the United States."

GAO will also be auditing the VA's financial statements for Fiscal Year 1987 and has hired an actuarial consultant to assist them in their review of the insurance statements. Our actuaries will be meeting with GAO's consultant this month to discuss the methodology and acutarial principles that are used by the VA in determining our reserve needs. We are hopeful that as a result of these discussions we can reach a mutually satisfactory agreement with GAO on the appropriate accounting principles to be used in valuating the reserve requirements for each program.

[Copy of report referred to appears at p. 49.]

Mr. APPLEGATE. One of the organizations mentions a problem with the insurance people timely notifying a veteran of his eligibility to apply for RH (Service Disabled Life) insurance. Could you explain how you notify a veteran of his eligibility to apply?

Mr. VOGEL. Yes, Mr. Chairman. When a rating decision is made, which establishes eligibility for a veteran to apply, a copy of the rating decision is sent to one of the two insurance centers for later contacting the veteran. We don't believe there is a significant problem with getting that notification in. From time to time I think it can happen that, through clerical inadvertence, a rating decision is not forwarded to the proper people.

As part of our general program to try to modernize our systems, what we are going to do is install an automatic notice. Since we use computers to help process our work, we will make the notice automatic and thereby prevent ourselves from making an error of not getting the rating sheet through. We see that from time to time, but we don't believe it's a prevalent problem. Any time it comes up we will and can, in fact, correct it.

The veterans' service organizations, who frequently have a power-of-attorney in such cases, notify us. They are part of the service equation and we can take immediate steps to remedy that.

Mr. APPLEGATE. Two other short questions.

One, we have had several calls and letters regarding a so-called "veterans ballot" that has been sent out by an insurance company, the Veterans Life Insurance Company, I think it may be called. Could you comment on the VA's response to this and what it is that you have found out?

Mr. VOGEL. Yes, I can, Mr. Chairman. We have received complaints about that mailing. We have advised individuals to contact the insurance commissioner of the respective States in which they reside. Mr. Koons or Mr. Carey may want to elaborate on the specifics of that so-called "veterans ballot."

Mr. CAREY. It is fairly clear that the "veterans ballot" is being used by the Veterans Life Insurance Company as a marketing device. It actually comes out of and under the control of their marketing department. They purchase mailing lists from various organizations. We have received some complaints and we have referred them to the Pennsylvania State Insurance Commissioner and the State from where the person complaining resides, since the regulating of insurance companies rests with the State.

In the past, the Veterans Life Insurance Company has had sanctions brought against it by the Pennsylvania State Insurance Commissioner. They have been fined and they have agreed, in all of their advertisements for insurance, to indicate they are not affiliated with a Government agency.

Mr. APPLEGATE. I think that should be noted. Is it an illegal procedure, or is it one that could be considered as unethical?

Mr. CAREY. I will turn that over to General Counsel.

Mr. THOMPSON. As Mr. Carey mentioned, the State Commissioner in Pennsylvania successfully brought sanctions against the company a couple of years ago because its advertisements looked too much as though they were emanating from a Government source. As to this current "veterans ballot", obviously we would again defer to the State authorities as to its legality.

It certainly does not appear to violate any Federal mail fraud statutes, but we have referred it to the Postal Service just to make sure on that count. We will be glad to advise the committee as to what we learn.

Mr. APPLEGATE. Okay. I would appreciate that.

One final question. We can disregard that red light on the table and leave this open, because we don't have that many members here.

Every once in a while we get letters from people who talk about the insurance dividend, and I'm sure each of the members of the committee here are aware of that. We get these letters and people expect to get a lot of money back in, so we do get a lot of inquiries. It's a hoax; that's what it is. But for the record, has the Veterans' Administration done any kind of investigation on this and, if so, what has been found out?

Mr. VOGEL. Mr. Chairman, we have looked for the source of that hoax numerous times. It almost has the characteristics of a phantom. It just springs up from time to time. It looks nice. It's published in employee newsletters from time to time. A chapter or a post of a service organization will put something in.

The major service organizations have published information about that hoax to their members, and we do very much appreciate that. We get about 4,000 per week in recent times, which means we tie all those employees up in telling people this is a hoax and there's nothing there. Thank goodness for word processing. We can at least do it with some dispatch. If we knew the source, we would take whatever vigorous steps are needed to cut it off.

Mr. APPLEGATE. If you could determine a purpose, then you could know the source. But I don't know what the purpose is because I don't know who profits by anything like this, unless it's just a direction of destruction of some sort.

Mr. VOGEL. We thought about that. It just seems as though—it got out once, and from time to time somebody picks it up and they just run with it. There is no way any individual that we could determine could ever profit by that. It unfortunately preys on the veterans who may have had coverage in the past and their coverage has lapsed or they discontinued paying premiums or whatever.

It's one of those deals that looks as though you can get something for nothing, and we all know that in the world of reality things don't work that way. If you have active insurance, you can

get dividends; if you don't have insurance, there is no way that dividends can be paid. We think it's a tragic thing and it raises false expectations among a number of our veterans.

Mr. APPLEGATE. It surely does. I thank you very much.

Mr. Penny.

Mr. PENNY. Thank you, Mr. Chairman.

I'm interested in an answer to the question I raised in my opening remarks; that is, what is the status of the plans for consolidation of the insurance centers, given the position the House has taken on that issue?

Mr. VOGEL. Officially, we intend to continue to proceed. Obviously, the measure that you introduced, if enacted, would bar us. We will, of course, abide by that.

We do believe that it did make good economic sense, that there were savings to be achieved. The GAO did a study and, unfortunately, they were looking at apples and we were looking at oranges. We have communicated officially our view on their methodology on what they looked at with respect to the cost benefit analysis.

I have said it before and will say it again. We have two very fine insurance operations. At one time we had 13. The St. Paul and Philadelphia employees and the management of those two operations are very, very fine. The effort that we made to effect a consolidation we thought would save money, and we still believe it will save money. It certainly was no reflection on the quality and type of employees and the manner in which they delivered insurance benefits at St. Paul. It was just that our analysis indicated it was more beneficial, cost-wise, to have a larger entity absorb a smaller, rather than a smaller absorb a larger.

We are very proud of the employees that manage the insurance programs throughout the United States. If ever I have seen one, that's a Government success story. But as of right now, our plans are to continue to proceed until such time as we're precluded from doing so, however that's effected.

You will recall last year, Mr. Penny, the Appropriations Committee, pending an analysis, indicated we could not expend appropriated funds to effect that transfer for the fiscal year they were addressing. Of course, we did nothing and waited for the GAO to make a report, which took them about a year-and-a-half, an awfully long time.

Mr. PENNY. You are aware that the Appropriations Committee has a similar provision in the HUD and Independent Agencies appropriations bill at this stage. That bill hasn't been reported to the House floor yet, but my understanding is that a similar prohibition is in the bill.

Mr. VOGEL. Yes, sir, I'm aware of that.

Mr. PENNY. Let's say that no legislation passes. What is the time frame under which this consolidation would occur if a restriction is not legislated?

Mr. VOGEL. It would begin October 1 and, over an 18 month period, we would migrate in various and sundry insurance activities from St. Paul to Philadelphia.

Mr. PENNY. What if no legislation were finalized by October 1 but an appropriations bill and an authorizing bill were hanging out

there likely to be adopted in the foreseeable future; would you hold things back until you had a clear signal, one way or the other?

Mr. VOGEL. I think that's the kind of situation where I would seek the counsel of the General Counsel and the comptroller himself, and probably the Administrator himself.

But I don't know exactly what we would do. My inclination would be to defer any action . While we plan to begin on October 1, if it happened a little bit later, I guess that's what we would do.

I might indicate that just the day before yesterday I visited the St. Paul Regional Office and the insurance operation there. It's a good office. In addition to being unique—there are only two insurance operations, and they're one of them—they also very effectively handle something we call the Centralized Accounts Receivable System. With a rather small number of employees, with heavy computer assistance, they have a very effective effort underway to try to recover moneys that were inappropriately paid to beneficiaries. The fact that the VA put that operation there is an indication of the faith in the quality of the people there and the quality of the management of that operation. I had the pleasure of spending the better part of a day with the director and his staff on Tuesday.

Mr. PENNY. There's no doubt they're good folks. I'm sure they would appreciate those compliments, and they would also appreciate some indication that their office isn't subject to closure.

I appreciate your answer. In just knowing the way things operate around here, there is a good chance we may end up with a CR and that may leave the appropriations measure for HUD and independent agencies hanging in the air awaiting final enactment sometime later in the fall. We don't know what the Senate might do on various veterans bills that we have already approved here in the House. So here again, we might be waiting beyond October 1 before an authorizing bill addressing this issue has been finalized. So I appreciate knowing that the likelihood is that you will hold in abeyance, or there is a good chance you will hold in abeyance any formal moves in that direction until you see what the action of Congress is.

Mr. VOGEL. That's my seat-of-the-pants reaction to that. As I indicated, I have no—

Mr. PENNY. Again, I know you have no authority within the VA to consult on that, but it seems to me that that's the direction you sense things will likely go.

Mr. VOGEL. Yes, sir.

Mr. PENNY. And I think that would be wise. Thank you.

Thank you, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. Penny.

Mr. Bilirakis.

Mr. BILIRAKIS. Thank you, Mr. Chairman.

Mr. Vogel, it is good to see you again, sir, and all of you gentlemen. Again, we thank you for the fine job that you're doing on behalf of our veterans in this area.

Before I get into the particular point I would like to concentrate on, maybe I could hitchhike on Mr. Penny's questioning. Once you close an office in the process of this consolidation, and realizing you would save money and theoretically maybe be more efficient

because of consolidation and whatnot, but what if it turns out not to be? If it turns out the veterans are being hurt as a result of that, then we have got to start all over again, I suppose. We're talking about not only not saving money but a heck of a lot more expense probably.

Has the VA considered or is the VA maybe now picking certain model areas where they would possibly consider closing those particular offices, but closing them in the sense that they would not be giving up the lease, et cetera, but sort of conducting the process as if the office were closed, in some way to see how efficient that would be and if veterans would be better served—you know, using that as a model, so to speak. Have you considered that, or are you doing it at all?

Mr. VOGEL. We have studies underway that determine the best manner in which to deliver the benefits. We have functionally consolidated certain activities over the passage of a long period of time . We have 58 regional offices, but we have 49 loan guaranty operations. For instance, the St. Paul office we were talking about a moment ago handles loan guaranty for the State of Minnesota and North and South Dakota as well. We have some rehabilitation activities that are run out of one State and they take care of an adjoining State. We are looking all the time to determine the best way we can do it.

Computer assistance and electronic linkages allow you to do a lot of things that were previously precluded. We can enhance even further our computer capabilities and our master records. We can do a lot more by linking people electronically in their work. We are looking now at the functional consolidation perhaps of a couple of loan guaranty activities that are found in the 49 regional offices that may be able to be handled at one, two or three because of electronic fund transfer and other areas.

There are a number of things underway. There is a management advisory committee in the Department of Veterans Benefits that is assisting me in looking at the notion of shifting workload. The tendency is to take small offices, small workloads, and move it to areas where workloads are larger, with staff flexibility and other things.

Because of what I referred to as essentially computer linkages, they are also looking at maybe moving, from large facilities to small facilities, some of that same work by moving it electronically. So there is all kinds of reiterations on it. We want to provide the best service we can, and we want to provide the same high level of due process in claims that we are now providing. As we go through these studies, we are cognizant of our responsibilities for responsive and timely service with full consideration to the veteran's rights to due process in matters affecting—

Mr. BILIRAKIS. Yes, sure, we're all concerned about due process in the processing and whatnot, and I know that computers can be very helpful there. But there is no substitute for that veteran being able to actually walk into a facility, a relatively local facility, and being able to discuss his problems. If that office is closed down, that veteran would not have that available. That is why I talk about some sort of a model type of thing.

Well, that's in your good hands. I would hope that we don't do something and it turns out really to have been a wrong move, and then it ends up costing a lot more and in the process we've lost an awful lot of face with our veterans.

Mr. Vogel, at the bottom of page 6 of your prepared testimony—and I know you have talked about it here, too, about the programs being generally self-supporting—and then you talk about title 38 requiring the U.S. to bear the costs associated with administering the programs. Then you refer to the net cost to the Government as $25,759,413. That is a cost that comes out of the Treasury, out of the VA budget. But is it a cost that goes to Government employees? When we talk about administration, it is the Government employees administering—

Mr. VOGEL. Yes, sir. It's the salaries of the people who manage those, the remittance processing equipment, the ADP equipment—

Mr. BILIRAKIS. None of that goes to private insurance companies; that's basically what I'm asking.

Mr. VOGEL. No, sir.

Mr. VOGEL. And that represents an average of $6.97, and you said that orally here also, per policy maintained for fiscal year 1986, right?

Mr. VOGEL. Yes, sir.

Mr. BILIRAKIS. So that cost, then, with the exception of the fact that you have cost-of-living expenses going up and whatnot, that cost is basically static on a per policy level.

Getting then to the problem, particularly with NSLI—and I'm familiar with it because I still have my NSLI policy. The veterans organizations also make the point I'm going to make very well in their prepared remarks, and I'm sure they're going to do it when they have the opportunity to come up here. $10,000 used to be worth something back in the Forties and Fifties. It's just almost nothing today. For many of these people, it's basically the only policy that they have, and for a number of reasons. Some of them just haven't been able to afford too much more.

Have we considered increasing that amount? I mean, have we seriously considered declaring some of those policies paid up at a certain age? I'm not as prepared as I should be maybe, and I don't have the ranges here, but every 5 years those premiums go up, and by the time you hit age 70 or something you definitely can't even afford $10,000 term life insurance because of the costs.

I might add at this point that we all receive dividends, and they're pretty good dividends. I'm not sure if we wouldn't be willing—at least I would be willing, and I imagine probably an awful lot of other veterans—would be willing to forego some of those dividends, if it took that, in order to help out some of these people who reach a certain age and have to basically give up their insurance.

Mr. VOGEL. Yes, sir. We have done a couple of things. We have declared USGLI policies paid up . That's essentially, mostly, World War I, and the policies were issued from 1919 to 1951.

We have made a study of the reserves to determine that we have enough on hand to pay all claims, so they pay no premiums any longer. The number of policies in that is still in the neighborhood of 56,000.

We have capped NSLI-term insurance. You mentioned that every so often the premiums go up. We capped the premiums at the age 70 rateso that it never goes higher, if they maintain that coverage, than it would be at the age 70 rate.

Mr. BILIRAKIS. Do you remember what that premium is off the top of your head for age 70?

Mr. VOGEL. It's $6.18 per thousand per month.

Mr. BILIRAKIS. Per month. Okay. So it gets up to what, $800 or $900 a year?

Mr. VOGEL. Yes. It gets expensive.

Mr. BILIRAKIS. Pretty rough.

Mr. VOGEL. For a lot of those individuals, term was a comparatively cheap form of insurance, but as you get older, you pay more for it. A number have converted to permanent plans of insurance, in which case the mortality experience has been so good that it is very low cost coverage. But one must maintain those in force to enjoy the benefits of dividends.

Mr. BILIRAKIS. But I'm speaking of the guy who doesn't convert it to the permanent plan. It seems like a simple thing to do, but I haven't done it yet. I keep planning to do it, but it seems 5 years just comes and goes and before I know it I'm going to be in that category.

Mr. VOGEL. We'll write you a letter, Mr. Bilirakis, to tell you exactly how much and when.

Mr. BILIRAKIS. I think you do that every 5 years.

Mr. VOGEL. Yes, sir, we do.

Mr. BILIRAKIS . To be practical and realistic about it all, we talk about the reserves that we have, and it is a good accounting practice, but the practicality of it all is that $10,000 just doesn't cut it any more, and the premiums at an advanced age are just fantastic. I think we have to take another look at that. I feel confident that we could do that in some way—because the administration costs apparently would remain the same. I should think we could come up with something like that without necessarily dipping into the Treasury for any additional amounts.

Mr. VOGEL. One thing that an insured can do is instead of taking the dividend check—some obviously need that check—allowing that to be used to purchase paid-up additions. We've had cases in which a $10,000 policy in force, with the dividends being used to buy paid-up additions, have yielded $20 to 30,000 in the face value of insurance at the time of the insured's death. That is one way to get increased coverage.

Mr. BILIRAKIS. Is that in the booklet, or is that in the premium notice that goes out periodically? I don't recall seeing that or reading it.

Mr. CAREY. It's in the booklet, sir.

Mr. BILIRAKIS. You see, I'm an attorney, I'm a Congressman, and I wasn't aware of that. I haven't read that booklet, which is my fault. I realize that there is only so much the Veterans' Administration can do, and as I have already said, you all are to be complimented for the job you are doing.

But I don't think it's practical to figure that all of those veterans there will have that booklet available, or will ask for that booklet, or really peruse it as well as they should. Maybe it goes back again

to the regional offices maybe not understanding, where somebody doesn't understand it and they want to go sit down and talk to somebody and the regional office is closed down. I think it's a realistic situation and we ought to face up to it. For many of these veterans—as has been said here many times in the past about other types of benefits—for many of these veterans it will be the only benefit that they will have gotten from their Government and from the Veterans' Administration in their lifetime for the service they gave to their country.

I think we ought to take another look at that. If there is some help through legislation that you all feel you would like to get from this committee, officially or unofficially, please let us know, because I think we really ought to take a serious look at it, Mr. Vogel.

Mr. VOGEL. Thank you, Mr. Bilirakis.

Mr. Koons advises me that we are now considering putting a stuffer in the mail to individuals, advising them of their ability to buy paid-up additions with dividends, rather than taking the dividend checks.

Mr. BILIRAKIS. I appreciate that very much. Let's do that, but let's also take a look at it from the standpoint of maybe we could reduce the dividends across the board—maybe some of the other veterans won't be happy about that—reduce the dividends across the board and apply that to a paid-up or a lower paid-up plan, something of that nature. But let's take a look at all sorts of alternatives there so that we can be more helpful.

Mr. VOGEL. We have considered that from time to time, and one of the service organizations has raised it regularly. We really look upon it as an equity issue. You take from a person who has been paying higher premiums for permanent plans of insurance, taking his dividend to somehow subsidize the individual who has retained term coverage at a lower cost all these years, then—

Mr. BILIRAKIS. All right. That's an argument, and it's a good argument, and obviously I have thought about that. But I think we ought to be looking at alternatives, and maybe that would be one of them.

You said a veterans organization has recommended doing that?

Mr. VOGEL. One of them that I can think of that does it regularly. Our response has been the argument from an equity position.

Mr. BILIRAKIS. And which veterans organization is that, do you remember?

Mr. VOGEL. I think it's the Reserve Officers Association.

Clearly, as you indicate, Mr. Bilirakis, and as they have, it gets awfully costly to maintain that insurance. The thrust of the suggestion, what they are trying to do, we think is laudable. But we have a problem with the equity issue. Certainly, as our actuaries look at the operation of the program, we have been endeavoring to do whatever we can to try to make more coverage available to more people at no more cost or less cost. We have been very successful over the years in doing that. But we would be pleased to consider—

Mr. BILIRAKIS. Okay. Basically, I don't think that we, the Congress, are in any ivory tower, that there is any way that we know as much about these subjects as you do. I don't think we should always be coming up with legislation and basically shoving it down

your throat. I mean, it's obviously necessary in many instances. H.R. 303 is intending to do that, and I don't know where you draw the line, either. But all I'm saying is it is a problem, a realistic, practical problem, and I would hope that the VA will be addressing it and hopefully coordinating with this committee.

Thank you very much, Mr. Vogel.

Thank you, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. Bilirakis.

Mr. Vogel, Mr. Thompson, Mr. Carey and Mr. Koons, I thank you very much for appearing before the committee. Of course, your entire testimony will be made a part of the record, along with the exhibits and the charts that you have submitted.

Mr. VOGEL. Thank you, sir, and thanks for having us.

Mr. APPLEGATE. The next witness we have is a familiar face, Mr. Bob Moran, who is Associate Legislative Director of the PVA. Robert, it is always good to have you here.

I might inform those who do not know that this is going to be the last time Bob will be appearing before the Veterans' Affairs Committee, at least in this capacity. Maybe at another time and another place you will be back.

For my own part, I would just say we will miss your smiling face around the halls. Nobody works the halls better. Nobody has more of an impact by their presence before the committee than you. I have five subcommittees and run through a lot of lobbyists, but there isn't anybody on the Hill that we have greater regard for or respect for. So we will miss having you around.

I'm sure you don't like to hear all of this, but being the Chairman, I can say it anyway, and you'll have to sit there and listen.

[Laughter.]

Mr. MORAN. I agree.

Mr. APPLEGATE. It's always good to have you here, and we will certainly welcome you back any time you want to enter those doors.

STATEMENT OF BOB MORAN, ASSOCIATE LEGISLATIVE DIRECTOR, PARALYZED VETERANS OF AMERICA

Mr. MORAN. Thank you very much. I wasn't nervous before I started, but now I am.

Let me say that yes, this is my last hearing. I will be in the area, so I look forward to coming back, and I thank you very much for those remarks. It really makes me feel good.

I am here representing the Paralyzed Veterans of America. Since most of the facts and figures are in our testimony, let me just briefly talk about two insurance programs that directly affect PVA members and myself personally.

Mr. Bilirakis was expanding on one of those programs, that being National Service Life Insurance, RH insurance. As you know, that insurance is for the service-connected veterans, and from PVA's standpoint, it is sometimes this service-connected disability that our members, the more catastrophically disabled, are unable to purchase additional insurance in the civilian market. So what we are advocating—and the facts and figures are in our testimony—is to raise NSLI, RH insurance, for that particular group, possibly

with a hundred percent rating or something—I'm not really sure on the particulars—but to raise that particular insurance for that particular group, say, from $10,000 to $50,000.

Our facts and figures prove that, based on age, income factors and dependents, that for the average spinal cord injured veteran, for his amount of insurance, it should be a little over $100,000. So for these veterans who are unable to purchase additional civilian insurance, $10,000 is very inadequate. Again, the facts and figures are in our testimony.

The other program I would briefly like to mention is Veterans Mortgage Life Insurance. In 1976 the average housing cost was about $58,000. With the grant and the VMLI protection, the veteran was pretty well assured of taking care of his family upon his death. Last year, in 1986, the average price of a home was about $112,000, and with the VA grant and VMLI, quite a portion is left over at the veteran's death. So we are advocating, since housing costs have risen, and VMLI has stayed at $40,000 since 1976, that you might take a look at raising that particular program, too.

I would like to comment and thank the VA for the implementation of their insurance programs. We feel they continue to serve the veterans. There was a provision in VMLI that came up, I think last year at a hearing, where there was a particular category of veterans where their VMLI fell under a certain level and they could not go back to the $40,000 limit when, in fact, if he bought another home in another area and needed that protection. That is in the process of being taken care of, so we want to thank the VA for that.

Again, in NSLI, RH, and VMLI, we just think the amounts need to keep abreast with the prevailing market on the outside.

That concludes my statement. I would be glad to respond to questions.

[The prepared statement of Mr. Moran appears at p. 79.]

Mr. APPLEGATE. Thank you very much, Bob.

I don't have any questions. We will certainly be reviewing your testimony, as we always do. If we do have any specific questions, we will write to the PVA and for their response.

Mr. MORAN. Thank you.

Mr. APPLEGATE. Mr. Bilirakis.

Mr. BILIRAKIS. Thank you, Mr. Chairman.

Well, Bob, that news comes as a surprise to me. I didn't know that you were leaving PVA. You're going to be missed in many ways.

I would like to note that Mr. Vogel is still in the room. I always like to make note of that because we have an awful lot of hearings in other committees, particularly Energy and Commerce, where people testify and then just get up and walk out and don't get the benefit of the other testimony.

Mr. MORAN. We're aware of that, too.

Mr. BILIRAKIS. But the Veterans' Administration people for the most part just stay in the hearing room and listen to the testimony. I think that's to their credit.

You brought up a point a lot more eloquently than I, and that is the fact that many of these veterans are disabled and they are not able to get insurance. So when we talk about some people stuck

with $10,000 life insurance, it's not always just because they can't afford it or because they haven't gotten around to it or whatever. Oftentimes they have tried and just haven't been able to do it. So we have to take that into consideration. I'm sure that Mr. Vogel has. It's just very critical that we address this situation.

Has the PVA determined any cost estimates for increasing the coverages from $10,000 to $50,000 and raising the mortgage insurance to 70? Have you all gone into that at all?

Mr. MORAN. We have started putting some figures together. We haven't really—We talk about raising NSLI RH for the service-connected. I think with the numbers that are out there, and with the costs that were mentioned today, that we're talking a pretty good dollar figure. I think what we're trying to do is more narrowly define what group we're talking about and we're trying to put the cost figures for that particular group. We don't have them as yet, but we're working on it.

Mr. BILIRAKIS. Thank you.

I have nothing further, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. Bilirakis. I, too, would like to commend Mr. Vogel and his associates for sticking around and listening to the testimony. This isn't the first time. They usually do that, and it is good that they get to hear the testimony first hand.

Bob, I have no other questions. I thank you once again for appearing before the committee. We always look forward to having you come back.

Mr. MORAN. Thank you.

Mr. APPLEGATE. Next we will have Mr. Gordon Thorson, who is Special Assistant, National Legislative Service, Veterans of Foreign Wars. Gordon, welcome to the committee again.

STATEMENT OF GORDON R. THORSON, SPECIAL ASSISTANT, NATIONAL LEGISLATIVE SERVICE, VETERANS OF FOREIGN WARS OF THE UNITED STATES

Mr. THORSON. Thank you, sir.

Chairman Applegate and members of the subcommittee, it is always a pleasure to appear and offer the position of the Veterans of Foreign Wars. Today's hearing was scheduled to review the current status of the VA insurance division and the programs that it administers. Our written testimony was previously submitted to the subcommittee for review and we ask that it be made a permanent part of the hearing record. I will be brief.

First of all, the Veterans of Foreign Wars would like to compliment the subcommittee for its continued efforts to monitor and improve the VA insurance program.

Secondly, we must compliment the Veterans' Administration on the success of the insurance programs they administer and the quality of the personnel assigned to each insurance center. Our department service officers at both centers have lavished much praise on the center directors and their staffs for the courtesy and cooperation they regularly demonstrate.

Mr. Chairman, we do have a few areas of concern, however. Our membership recently met in New Orleans, LA. at the national convention and passed a resolution calling for the retention of the St.

Paul Insurance Center in Minnesota. It has been suggested that consolidation with the Philadelphia center would not result in a savings to the Federal Treasury, nor would the move result in improved service to veterans. We realize that the House Veterans' Affairs Committee and the full House has passed legislation to safeguard the St. Paul center, and we applaud your actions.

Secondly, the VFW would like to direct the committee's attention to mortgage insurance for certain disabled veterans. Too often veterans suffering from a service-connected disability, who are not entitled to special adaptive housing allowance, cannot obtain mortgage protection life insurance, other than high-risk insurance, which carries very high premium rates. All too often these rates are beyond the veteran's financial capability.

We would support the introduction and passage of legislation that would provide affordable mortgage insurance to this special group of veterans, thus allowing them an opportunity to provide their families with the security of a mortgage-free home if they should die.

Finally, we suggest that the VA Central Office should take a good close look at regional office notification procedures as it applies to RH National Service Life Insurance. We have had reports on notification delays at some regional offices and ask that our concerns be reviewed. Our concern is to ensure that the veteran be allowed the full 1-year grace period provided under law and provide him with the information necessary to make an intelligent decision in a timely fashion.

Thank you. That completes my testimony, sir.

[The prepared statement of Mr. Thorson appears at p. 85.]

Mr. APPLEGATE. Thank you very much, Gordon. I appreciate that. We will certainly take under consideration the concerns that you have expressed here. I don't know what the resolutions will be on it, but we will certainly be looking into it.

I think the Veterans' Administration has answered it, at least to their own satisfaction, and if there is an equitable solution to the problem, we will certainly be working along with you to supply that solution.

Mr. THORSON. Thank you, sir.

Mr. APPLEGATE. Mr. Bilirakis.

Mr. BILIRAKIS. Thank you, Mr. Chairman.

I would ask maybe the same question. Has the VFW taken into consideration the costs, or do you have any cost estimates on these changes that you're proposing?

Mr. THORSON. No, sir, we haven't.

Mr. BILIRAKIS. So you really can't answer as to whether you think it might take new dollars, or whether it possibly could be handled within the current program.

Mr. THORSON. No, sir. We haven't looked into that.

Mr. BILIRAKIS. Again, Mr. Vogel is still here with his troops. I know they have heard your testimony. Again, we plead on your behalf and on behalf of our veterans, particularly our disabled veterans, that they take all these things into consideration to stave off any legislation. I just don't think we know enough about this subject to actually have to legislate it.

Again, if you, the VFW and PVA, have any suggestions in terms of terminology and whatnot that can be used towards legislation, we would like to hear that.

Thank you very much, Mr. Thorson.

Thank you, Mr. Chairman.

Mr. APPLEGATE. Thank you, Mr. Bilirakis. And again, thank you, Mr. Thorson, for appearing before the committee.

There are no other witnesses to testify before the committee, and because of that, the meeting is adjourned.

[Whereupon, at 10:13 a.m., the subcommittee was adjourned.]

APPENDIX

Statement of

R.J. VOGEL

Chief Benefits Director

before the

Subcommittee on
Compensation, Pension and Insurance

House Committee on Veterans' Affairs

September 10, 1987

Mr. Chairman and Members of the Subcommittee:

We appreciate and welcome the opportunity to address the Subcommittee and provide you with the current status of the government life insurance programs that are supervised and administered by the Veterans Administration. We will focus our remarks in particular on the changes that we have implemented since the last insurance oversight hearings, and on our current initiatives to enhance each program's benefits and to improve our administration of the programs.

In terms of size, the Veterans Administration's life insurance programs currently provide over $209 billion in insurance protection to 7.4 million veterans and members of the uniformed services. In the commercial life insurance industry, the Veterans Administration would rank as the fifth largest life insurance company when comparing the total amount of coverage which is provided.

From a financial standpoint, all of the programs that were designed to be generally self-supporting are in sound financial position. The two programs which insure the lives of disabled veterans at standard premium rates, Service Disabled Veterans Insurance (SDVI) and Veterans Mortgage Life Insurance (VMLI), continue to require annual subsidies from appropriated funds as expected.

I will now briefly discuss the status of each of the individual programs that are administered by the VA.

The United States Government Life Insurance (USGLI) program (policies prefixed with K) was established in 1919 to provide insurance protection to World War I veterans and active duty members of the Armed Forces. A total of 1.25 million policies were issued under the program, which was closed to new issues in 1951. There are over 56,000 USGLI policies in force today. Unlike most of our other administered programs, which are still on a premium paying basis, the USGLI program was declared paid-up as of January 1, 1983. Since our actuaries determined that the program's reserves and future earnings were sufficient to meet all of the future liabilities of the program, no further premium payments are required from these policyholders. The average age of the USGLI policy-holder is now 79 years, and consequently the death rate for this group is the highest of all of the programs at 97.6 deaths per 1,000 policyholders.

The National Service Life Insurance (NSLI) program (policies prefixed with V, H, N, AN) was authorized by the NSLI Act of 1940. As a result of the many amendments and expansions of the NSLI program, there are now four distinct NSLI programs. The largest program is the "V" insurance program which was open to new issues between 1940 and 1951. During that eleven-year period, over 22 million policies were issued with over 2.9 million policies still remaining in force today. The average age of this group is 64 years.

Approximately 30 percent of these 2.9 million policies represent term insurance coverage. As we reported at the last oversight hearings, the premiums on these term policies were capped at the age 70 rate of $6.18 per month per $1,000 of coverage on September 1, 1984. The reserves required to support this initiative were derived entirely from funds contributed by term policyholders. As of December 31, 1986, 80,848 of the over 100,000 term policies were capped at the age 70 premium rate. Approximately 180,000 additional term policies will be capped at the age 70 rate within the next five years.

The Veterans Special Life Insurance (VSLI) program (policies prefixed with RS or W) was enacted in 1951 to meet the insurance needs of the Korean conflict veteran. Of the over 800,000 VSLI policies issued prior to the program's close in 1956, 354,745 remain in force today. The average age of this group is 54.

For a one-year period beginning in May 1965 and ending in May 1966, the NSLI program was reopened and a third type of NSLI, Veterans Reopened Insurance (VRI) (policies prefixed with J, JR, JS) was established for certain Korean and World War II veterans. As of the end of 1986, 132,265 policies of the 227,882 policies originally issued still remained in force. As a result of favorable mortality experience and high yield on the program's investments, we began paying termination dividends in addition to the regular annual dividends as of January 1, 1985, on JR and JS policies that are terminated by death, cash surrender, or maturity (endowment policies.) These termination dividends are being paid to ensure that the programs' assets are equitably distributed to policyholders and their beneficiaries as the program winds down. There are only 16,486 JR and 190 JS policyholders remaining in the program.

The Service Disabled Veterans Insurance (SDVI) program (policies prefixed with RH, ARH) is the only NSLI program still issuing new policies. Approximately 4,000 new policies are issued per year. There are presently 182,871 policies in force. A total of 304,429 policies have been issued since the program's inception in 1951. SDVI was made available to veterans who were discharged from active duty after April 25, 1951, and were suffering from a service-connected disability. The program insures medically substandard lives at standard premium rates; therefore, the premium income is not sufficient to cover all of the program's costs. In order to cover the excess cost of SDVI claims, a transfer is made from the Veterans Insurance and Indemnities (VI&I) appropriation. The subsidy required for fiscal year 1986 amounted to $7,796,000, bringing the total Government contribution since the inception of the program to $112,341,677. Unlike most other programs of insurance which hold reserves to cover the programs' future claims costs, the SDVI has no reserves to fund the program's future liabilities. Consequently, assuming that all SDVI policies are carried to their maturity, there is an unfunded liability which our actuaries estimate to be $629 million.

In administering these government life insurance programs, we have developed several initiatives that will enhance the financial benefits provided by these programs and improve the delivery of services to our policyholders and their beneficiaries. I would like to address these enhancements as well as briefly discuss the projects underway that are intended to modernize the technology designed to deliver insurance benefits and services.

A financial benefit enhancement that is now in the final stages of implementation involves the interest rate on new National Service Life Insurance (NSLI) policy loans. A proposed regulatory amendment was published in the Federal Register on June 11, 1987. We expect the final rule to be published in the near future. The new regulation provides for a variable interest rate on all new NSLI loans. The initial rate will be set at 8 percent per annum and will remain in effect at least through September 1988. Thereafter, the interest rate will be adjusted depending on the performance of an economic indicator. The indicator is the June interest rate for U.S. Treasury Securities, 10-year constant maturities. The indicator will be reviewed each year and an adjustment will be made whenever the indicator rises above the next whole number or falls below the current rate. For example, if

the indicator rises to 9.2% in June of 1988 the policy loan interest rate would be raised to 9% in October 1988. If the indicator falls to 7.55%, the policy loan interest rate would be dropped to 7%. The interest rate will always be rounded down to the next whole number and will take effect on October 1st of each year. The variable policy loan interest rate will have a maximum ceiling of 12 percent and a minimum floor of 5 percent. We believe that a variable loan rate with the use of an economic indicator is a more equitable method of determining interest rates in that it allows us to bring earnings on loans more in line with the earnings on other trust fund investments. Since dividends for all policyholders are based in part on the investment earnings of the programs' reserves, this action will ensure that both borrowers and non-borrowers are treated the same for dividend distribution purposes.

Another benefit enhancement that was implemented on January 1st of this year was a change in the mortality and interest reserve assumptions that are used to determine the amount of paid-up additional insurance that a policyholder can purchase with his annual dividend. As a result of this action we were able to increase the face amount of existing NSLI paid-up additional coverage by approximately 15 percent. The amount of the actual increase for each individual policy is dependent on the age of the policyholder and the plan of insurance. In addition to the one-time increase in coverage, policyholders who elect to use their dividends to purchase paid-up additional insurance will now be able to purchase approximately 15 percent more of this type of coverage with each dividend dollar than they were able to purchase prior to January 1, 1987.

We were able to take this action because of favorable mortality experience and the sustained high yields on our investments. The increase is supported entirely by the reserves maintained for paid-up additional coverage. Approximately 810,000 NSLI policies initially benefited by the increase. The total dollar value of the one-time coverage increase was approximately $350 million.

Among our current legislative initiatives is a proposal, which has been included in HR 2008, which would grant the Administrator the authority to periodically increase the amount of the monthly installment payments to beneficiaries who are receiving insurance proceeds under one of the annuity options. We were able to recommend this action because of the high yields on the invested reserves that have been held for payment of the NSLI "V" annuity settlements. We are currently required by Title 38 to use a 3% interest factor in determining the amount of each monthly annuity payment. The reserves that are being held for this purpose on the other hand are currently earning interest at the rate of 9.5% in the NSLI (V) portfolio. If the proposed legislation is enacted, we plan to increase "V" policy annuity payments by 50 percent for the next five years. Subsequent adjustments will depend on future interest earnings and mortality experience. This proposal would initially benefit approximately 130,000 beneficiaries at no cost to the Government.

We have also taken several administrative actions to improve the delivery of our insurance services and benefits and reduce our operating costs.

During the past two years, we have made progress toward our goal of redesigning and upgrading the Automated Data Processing (ADP) system which supports the Insurance program. Phase I of the Redesign Project, the inquiry phase, was completed in 1985. Phase II, the data entry phase, has been partially installed. We now have the capability to process on-line policy loans, address changes, and requests to pay premiums through an allotment or a deduction from a VA benefit payment. The most important advantage of having an on-line data entry system is its ability to edit and correct transactions before they are submitted for processing. This editing capability helps to substantially improve the quality and timeliness of our manually prepared input transactions. We estimate that Phase II of the Insurance ADP Redesign Project will be completed by March 1989.

An equally important aspect of our ADP redesign project is the conversion of our ADP programs from an outdated programming language into a modern programming language. This part of the project is being done by a contractor and is scheduled for completion by the end of next year. When the converted programs are installed, we expect to be able to implement several program modifications that will remove the current system restrictions which necessitate significant amounts of clerical intervention in order to process certain insurance ADP transactions.

Another administrative action that is currently in the planning stage is the installation of an "800" toll-free telephone number for use by government life insurance policyholders and their beneficiaries. Our cost/benefit analysis of toll-free telephone service for insurance service indicated that recurring annual savings of $200,000 could be achieved by installing an "800" number for insurance inquiries and requests for service. When installed in conjunction with our redesigned insurance ADP system, "800" service would allow policyholders to obtain up-to-date information and service on their insurance account in a matter of minutes. We plan to begin offering this service by early 1988.

As managers of the insurance trust funds, we have pursued an aggressive program of cash management and developed several initiatives that are aimed at ensuring that insurance remittances are received, processed and deposited in our Treasury accounts as quickly as possible. Timely deposits minimize float and allow maximum interest earnings on the insurance trust fund investments. In addition, many of our initiatives afford the policyholder more flexibility in terms of payment methods while reducing the administrative expenses associated with processing remittances.

We reported during the last oversight hearings that we were in the process of replacing our outdated remittance processing system. The new equipment was installed in September 1986, and became operational on October 1st of last year. Since the new equipment was acquired, we have been able to reduce staffing in our insurance collections activity by 35 percent, and still maintain our processing standards. We currently deposit 95% of our insurance payments in the Federal Reserve Bank on the same day they are received.

Along with the acquisition of the new remittance processing equipment, we have developed three other cash management initiatives. Two of these initiatives, which involve mailings to policyholders, are presently underway. One of the mailings, targeted at those policyholders who pay their premiums monthly, encourages them to consider paying their insurance premiums on a quarterly, semiannual or annual basis. The initial mailing to policyholders who pay premiums monthly began in October 1985 and ended in September 1986. Eleven percent of those who received the mailing responded by changing their monthly mode of payment to one of the three alternative payment modes. This resulted in a reduction in remittance processing costs of more than $47,000 per year. In addition to paying a discounted premium, paying premiums on an other than monthly basis can also save the policyholder banking charges and postage costs. Because of the success of the initial mailing, we began a second mailing to policyholders in February 1987.

A second mailing directed to policyholders who receive a monthly compensation award from the VA encourages them to choose the option of having their premiums paid by a deduction from their VA benefits. Policyholders who elect to pay their premiums in this way benefit by saving checking and postage costs and are protected from inadvertent failure to make a premium payment on time. According to the latest statistics, approximately 30 percent of those who have received the mailing have opted to pay their premiums by a deduction from their VA benefit payment. The full mailing is expected to be completed in September 1988.

The third cash management initiative concerns the implementation of a preauthorized debit method of premium payment. The policyholders who elect to pay premiums by this option authorize us to draw a monthly premium payment

directly from their checking account. We expect to have the ADP support necessary to process payments in this manner installed by December 1987. We will begin inviting policyholders to apply for this payment method in early 1988.

I began my testimony today by stating that the Insurance programs were in sound financial condition. At this time, I would like to discuss in more detail the financial status of these programs.

The Insurance trust funds were established to ensure that each program is adequately funded to meet all future liabilities. On an annual basis, our actuaries determine the amount of reserves that must be set aside in order to meet anticipated claims. Any surplus funds are returned to the policyholders in the form of their annual dividend. The reserves are accumulated through premium collections and interest earnings. Ninety-one percent of all reserves are invested in U.S. Securities; the remaining 9 percent have been loaned to policyholders.

By law, trust fund investments must be exclusively in Federal government obligations. The Treasury investments are credited with interest on a semiannual basis. The yield on each block of Treasury securities is set at the time of purchase and remains fixed through maturity. The portfolio is arranged so that approximately one-fifteenth of the securities will mature each year. Although commercial insurance company portfolios are more diversified, the average rate of return on our investments in U.S. Treasury securities in 1986 (9.44 percent) exceeded that of the before-tax rate of return on the aggregate assets of commercial life insurance companies, which was 9.35 percent for the same period.

In a matter related to the financial management of the Insurance programs, the General Accounting Office (GAO) conducted an examination of the Veterans Administration's consolidated financial statements for fiscal year 1986. Their review disclosed that internal controls over Insurance programs were functioning properly. They also noted that the Insurance Performance Review and the Statistical Quality Control Programs are generally well developed and functioning properly.

Although the USGLI, NSLI, VSLI and VRI programs are generally self-supporting, Title 38, U.S.C., requires that the United States bear the costs associated with administering the government life insurance programs. The one exception is the Veterans Reopened Insurance (VRI), which is totally self-supporting.

During al year 1986, the total administrative cost attributable to the insuran programs was $27,314,052. Of this amount, $319,381 was reimbursed from the SGLI fund for supervision of the Servicemen's Group Life Insurance (SGLI) and Veterans Group Life Insurance (VGLI) programs. A total of $1,235,258 was reimbursed from the VRI fund as required by law for administration of the VRI program. The net cost borne by the Government was, therefore, $25,759,413. This represented an average of $6.97 per policy maintained for fiscal year 1986.

Before I begin my discussion of the insurance programs supervised by the Veterans Administration, I would like to briefly discuss the service we have been able to provide to our policyholders and their beneficiaries during the last year. As noted by the GAO during their recent review, we operate a Statistical Quality Control program at both Insurance Centers that covers all aspects of insurance processing. Although all insurance processes are subject to quality review, we recognize that the timely and accurate processing of certain end products such as loans, cash surrenders, death benefits, and disability awards is particularly important to our policyholders and their beneficiaries. I am proud to report that in the prior 12-month period, 95 percent of all death claims were paid within 10 workdays of the receipt of the claim and supporting documentation, 94 percent of all loans were granted within 5 workdays, 93 percent of all cash surrenders were processed within 6 workdays, and 86 percent of all disability claims were processed within 10 work days of receipt of a claim for benefits.

At this point, I would like to shift the focus of my discussion to the insurance programs supervised by the VA. They include the SGLI and VGLI programs and the VMLI program.

The SGLI program insures the largest group of individuals, with 3,477,000 members of the uniformed services, the ready reserves and the retired reserves representing a total face amount of coverage of approximately $173 billion. The insureds are covered by a group policy purchased by the VA from the Prudential Life Insurance Company of America, which administers the program from the Office of Servicemen's Group Life Insurance (OSGLI), in Newark, New Jersey. The premiums collected under the SGLI program are sufficient to cover all of the program's cost, except those costs that are attributable to extra mortality due to the hazards of military service. The law requires that the military services pay these extra hazard costs from their appropriation for active duty pay. No extra hazard payments, however, have been required from the uniformed services since 1975.

There have been several coverage expansions and coverage amount increases since 1965 when the SGLI program was instituted. Since our last oversight hearings, Public Law 99-166 was enacted. This law, which went into effect on January 1, 1986, increased SGLI coverage from a maximum of $35,000 to a maximum of $50,000 for all individuals on active duty and members of the ready reserve. This change resulted in an automatic increase in coverage of over $52 billion.

During the last oversight hearings, we discussed the reduction of the SGLI premium rate from $.116 to $.08 per $1,000 of coverage which went into effect in July 1984. We stated that the new premium was set below the "break-even" rate in order to reduce the contingency reserve to an appropriate level. The reserve level had risen above the required level primarily due to a sustained period of high interest earnings on the programs' investments. We anticipated at that time that an increase in the premium rate would be required this year as the reserves would be drawn down to supplement the premium income. I am pleased to report, however, that due to the excellent financial position of the SGLI program, a premium increase for the active duty and ready reservists will not be necessary in the near future.

One of the groups covered under the SGLI program is a relatively small group of retired reservists. Unlike the active duty members and ready reservists, the premiums paid by the retired reservists do not cover all of the program's costs. Consequently, an annual transfer from the basic SGLI fund is required to supplement the premium income. For the policy year that ended on June 30, 1986, over $9 million was transferred to cover the cost of insuring the 27,315 retired reservists in the program. A large portion of last year's subsidy was required to increase the reserve levels required to support the increase in maximum coverage to $50,000. Cumulatively, over $55 million has been transferred from the basic SGLI fund. We recently developed a proposal to restructure the premium rates for this group. The proposed rates, which have been forwarded to the Department of Defense (DOD) for their comments, have been structured so that each age group insured under the Retired Reservist program will at least bear its own mortality costs.

One of the current legislative initiatives which involves the SGLI program is our proposal to amend the SGLI statutes to exempt the program from paying state premium taxes. The rationale for this change is that SGLI, as a federal program, should be exempted from state taxation just as the the Federal Employees Group Life Insurance (FEGLI) program has been exempted by legislation from paying state premium taxes. Any savings occurring from this legislation would be passed on to the insured members. Since the SGLI program's inception in 1965 through December 1986, approximately $53 million has been paid in state premium taxes. This proposal has also been included in H.R. 2008.

To help improve the cash management of the SGLI program we have established an electronic funds transfer (EFT) system for SGLI premium payments, which are received by the VA from the uniformed services, and subsequently transferred

to the OSGLI. This electronic link was installed in October 1986. An EFT system for these payments eliminates the delay that results from sending these payments through the mail. Any delay in this transfer translates into lost interest to the SGLI fund. We are currently exploring the feasibility of establishing a similar link between the VA and the service departments which would allow the premium payments made by the Defense Department to be electronically deposited in the SGLI revolving fund.

One closing note regarding the SGLI program; two military tragedies have occurred since our last opportunity to present testimony. The crash of the airliner carrying U.S. Government troops in Gander, Newfoundland, occurred in 1985 and the attack on the U.S.S. Stark occurred earlier this year. Between the two incidents, there was a total of 285 casualties, with only one of these individuals not covered by Servicemen's Group Life Insurance at the time of his death. We attribute this high coverage rate to the automatic coverage feature of the SGLI program. In each of the incidents described above, OSGLI implemented procedures to expedite the payment of these claims. Policy proceeds were authorized by OSGLI in each case no later than one day after the receipt of all the necessary documentation.

In the Veterans Group Life Insurance Program we are currently insuring approximately 240,000 veterans and members of the Individual Ready Reserve and Inactive National Guard for $8.6 billion in insurance coverage. Like the Retired Reservist SGLI program, the VGLI program requires a transfer each year from the basic SGLI fund because the premiums collected have not been sufficient to cover the mortality and expense costs. During policy year 1986, $4.2 million was transferred from the basic SGLI fund, bringing the cumulative transfer since the program's inception to over $130 million.

Prior to the enactment of Public Law 99-166, on December 3, 1985, VGLI was available only to recently separated veterans and a small group of reservists who were rendered uninsurable at standard premium rates as a result of a service connected disability. The new law extended VGLI coverage to members of the Individual Ready Reserve (IRR) and the Inactive National Guard (ING). In order to notify individuals in the IRR and ING of their eligibility for this insurance, the Department of Defense provided us with a mailing list for these two groups. Of the over 420,000 applications mailed to those members on the DOD listing, 47,000 or 11 percent were returned by the post office as undeliverable. Only 3.6 percent applied for coverage.

One of our concerns in the VGLI program in recent years has been the sharp decline in participation in the VGLI program. Within the last two years we have taken several actions in cooperation with OSGLI to reverse this trend.

The first initiative involves allowing separating servicemembers to enroll in the VGLI program at the time of separation and to have the initial premium payment deducted from their final service pay. This initiative is being tested at the Fort Dix Separation Center where a film developed by OSGLI regarding the benefits of VGLI coverage is being shown to separating members. The results of the test show that 70 percent of those offered the opportunity to apply for VGLI are taking the coverage. If these individuals opt to have the entire first year's premium deducted from their separation pay, they receive one year's coverage at a discounted rate. We are now involved with Defense Department officials in planning the implementation of this enrollment process at major separation transfer points around the country.

We also restructured the VGLI premium rates. Since its inception, the VGLI program had two premium rates, one for age 34 and under and another for age 35 and over. Our actuarial staff, together with Prudential's actuaries, developed a new premium rate structure for individuals separated on or after July 1, 1986. The structure has six age brackets with the rates designed to cover the mortality expenses and administrative costs for each age group. The new rates represent a reduction of nearly 30 percent for the youngest age group insured under the program, which comprises about 80 percent of

separating service-members. The new rates were designed to both reduce the SGLI subsidy and to encourage the younger and healthier age group to participate in the program.

To afford VGLI insureds with some additional premium payment options we are currently working with OSGLI and the service departments to allow for the payment of VGLI premiums by an allotment from service retirement pay. We believe that the allotment method of payment for a group of individuals who are accustomed to having deductions made from their pay could be an inducement for them to purchase VGLI. It would virtually eliminate the possibility of lapse and it will reduce operating expenses. At the present time, the allotment option is available to both Army and Air Force retirees. Forty percent of those eligible for this option have elected to pay their premiums by allotment. We estimate that the remaining services will be able to offer this option by October 1987. We are also exploring the possibility of expanding this program to allow for deduction of VGLI premiums from VA benefits. At our request OSGLI is also in the process of implementing a discounted annual premium payment option in lieu of monthy premium payments. This annual payment mode will be offered to VGLI insureds beginning in October 1987.

As a result of these actions, the participation rate in the program increased from 19.6% in policy year 1985 to 23.8% in policy year 1986 and we expect it to continue to rise as our new initiatives are fully implemented.

The last of the three supervised programs of life insurance that I will discuss is the Veterans Mortgage Life Insurance (VMLI) program. The program has been administered by Bankers Life Insurance Company of Nebraska since the program's inception in 1971, through the Office of Veterans Mortgage Life Insurance (OVMLI), which is located in Lincoln, Nebraska. The VA supervises the program. The program provides up to $40,000 in mortgage life insurance protection to veterans who receive housing grants for specially adapted homes.

Our legislative program for the current session also includes a proposal which would allow the VA to directly administer the VMLI program. The annual savings that are expected to be derived by transferring this function in-house are estimated to be in excess of $95,000. We believe this proposal would enhance program efficiency and reduce costs without affecting the benefits provided by the program. This proposal is also included in H.R. 2008.

As of July 1987, there were 5,568 active VMLI accounts, representing approximately $183 million in coverage. Since the inception of the program, 2,966 claims have been paid, representing $61.5 million. The Government bears the administrative costs of the program and all costs for claims in excess of premiums paid by the insured veterans. The total Government subsidy for calendar year 1986 amounted to $4.4 million.

Mr. Chairman, this concludes my prepared remarks. I would be happy to answer any questions you may have.

Office of the Chief
Benefits Director

Washington, D.C. 20420

Veterans
Administration

In Reply Refer To:

Honorable Douglas Applegate
Chairman, Subcommittee on Compensation
Pension, and Insurance
House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

I have enclosed a set of exhibits that we have prepared for the committee's files which complement the testimony that we have submitted for the record at the oversight hearings held on September 10, 1987, by the House Veterans' Affairs Subcommittee on Compensation, Pension and Insurance. The exhibits provide statistical summaries on each of the life insurance programs administered and supervised by the Veterans Administration as well as investment data on the Insurance Trust Fund.

We appreciate having the opportunity to appear before the Subcommittee on Compensation, Pension and Insurance to discuss the current status of the insurance programs and the initiatives that we have taken to enhance the programs' benefits and improve the delivery of the insurance services that we provide.

Sincerely yours,

R. J. VOGEL
Chief Benefits Director

Enclosures

78-835 0 - 87 - 2

INDIVIDUAL PROGRAM SUMMARIES

VA ADMINISTERED INSURANCE PROGRAMS

UNITED STATES GOVERNMENT LIFE INSURANCE	EXHIBIT A-1
NATIONAL SERVICE LIFE INSURANCE	EXHIBIT A-2
VETERANS SPECIAL LIFE INSURANCE	EXHIBIT A-3
SERVICE DISABLED VETERANS INSURANCE	EXHIBIT A-4
VETERANS REOPENED INSURANCE	EXHIBIT A-5

EXHIBIT A

UNITED STATES GOVERNMENT LIFE INSURANCE

(Policy Numbers Prefixed With "K")

The War Risk Insurance Act of 1917 authorized the issuance of yearly renewable term policies to service personnel in amounts ranging from $1,000 to $10,000. These policies were issued from October 6, 1917, until June 7, 1924, when authority for their issuance was rescinded by act of Congress. During that period, approximately 4.4 million policies were issued for a face amount of over $40 billion of insurance. The final expiration date for any yearly renewable term policy not converted to a permanent plan or a five-year convertible term policy was July 2, 1927, unless the policyholder became disabled prior to that date.

The USGLI program was established in 1919 to handle the direct issuance of new permanent plan policies and conversions from War Risk term insurance. Very few new USGLI policies were actually issued until after June 7, 1924, however, when the issuance of War Risk term policies was terminated. New insurance could only be issued upon entry into the services until May 29, 1928, when the law was amended to permit anyone, in or out of service, who served honorably during World War I, to apply for new insurance at any time. The USGLI program was closed to new issues on October 8, 1940, except for World War I veterans who could apply for such coverage until April 25, 1951.

A total of approximately 1.15 million USGLI policies were issued, of which about 600,000 were in force in 1940 when the program closed to new issues for all but World War I veterans. The amount of insurance in force is currently decreasing at the rate of 9.0 percent per year. As of December 31, 1986, only 56,830 of the original 1.15 million USGLI policies issued still remain in force.

Program Statistics:

Opening Date	September 29, 1919
Closing Date (Non-World War I Veterans)	October 8, 1940
Closing Date (World War I Veterans)	April 24, 1951
No. of Policies Issued (new issues and conversions from War Risk Term Insurance)	1,153,000
Face Value of Policies Issued	$4,857,600,000
Average Amount Per Policy Issued	$4,213
No. of Five-Year Term Policies in Force	342
No. of Permanent Plan Policies in Force	56,488
Face Value of Policies in Force	$217,185,043
Average Amount Per Policy in Force	$3,822
Average Attained Age in 1986	78.8 years
Average Annual Death Rate	97.6 per 1,000
Total Investments of USGLI Fund	$266,202,094
Average Rate of Return on All Investments (As of December 31, 1986)	7.07%
Total Disbursements in 1986	$49,232,505

EXHIBIT A-1

NATIONAL SERVICE LIFE INSURANCE

(Policy Numbers Prefixed with "V," "H," "N" or "AN")

The imminence of large scale military inductions prior to World War II resulted in the enactment of legislation on October 8, 1940, which created a new insurance program known as National Service Life Insurance (NSLI). This legislation also closed the United States Government Life Insurance (USGLI) program to new issues for all but World War I veterans. The NSLI program was established in order to protect the USGLI fund surplus from depletion due to wartime claims and to permit updated total disability and beneficiary selection provisions. Incoming service personnel who met the good health requirements were eligible to apply for the issuance of five-year, non-renewable term policies in sums ranging from $1,000 to $10,000, which were convertible to permanent insurance after one year.

The end of World War II brought several changes similar to those which occurred after World War I. The Insurance Act of 1946 provided the following:

a. Removal of restrictions on beneficiary selection

b. Expanded optional settlements, including lump sum

c. An optional total disability income provision

d. Additional permanent plans available for conversion from term insurance

e. Availability of insurance to World War II veterans who were no longer in service

f. Availability of insurance to World War II veterans lacking coverage due to a service-connected disability less than total in degree

Subsequent legislation provided that permanent plan insurance could be issued without preexisting term coverage and that the term policies in force could be indefinitely renewed. The Insurance Act of 1951 closed both the NSLI and USGLI programs to new issues on April 24, 1951.

Over 22 million policies were issued under the NSLI program, of which 2,986,721 remain in force, for a total amount of $18,800,267,953 of insurance coverage.

Included in the 2,986,721 total NSLI accounts are 2,900 "H" accounts. This insurance was issued between August 1, 1946, and December 31, 1949, to certain veterans with service-incurred disabilities. This insurance has the same premium rates and policy provisions as "V" insurance except that the policyholders do not receive dividends.

Program Statistics:

Opening Date	October 8, 1940
Closing Date	April 24, 1951
No. of Policies Issued	22,177,000
Face Value of Policies Issued	$173,765,000,000
Average Amount Per Policy Issued	$7,835
No. of Five-Year Term Policies in Force	878,053
No. of Permanent Plan Policies in Force	2,105,768
Average Amount Per Policy in Force	$6,296
Average Attained Age in 1986	63.7
Average Annual Death Rate	19.9 per 1,000
Total Investments of NSLI Fund	$11,068,609,558
Average Rate of Return on All Investments (As of December 31, 1986)	9.15%
Total Disbursements in 1986	$1,596,133,780

EXHIBIT A-2

VETERANS' SPECIAL LIFE INSURANCE

(Policy Numbers Prefixed with "RS" or "W")

In order to meet the insurance needs of the Korean conflict, the VSLI program was established in 1951. It provided for the issuance of Veterans Special Life Insurance upon termination of active duty to veterans who had been covered by the Servicemen's Indemnity Act.

Insurance under the VSLI program was available, without medical examination, to veterans separated from service on or after April 25, 1951, and before January 1, 1957. Application had to be made within 120 days after separation, and insurance was available in amounts up to $10,000, less any existing NSLI or USGLI. Approximately 800,000 policies were issued, of which 354,745 remain in force for a total amount of $2,988,386,321 in insurance coverage.

Program Statistics:

Opening Date	April 25, 1951
Closing Date	December 31, 1956
No. of Policies Issued	803,111
Face Value of Policies Issued	$7,349,178,500
Average Amount Per Policy Issued	$9,151
No. of Five-Year Level Premium Term Policies in Force	31,351
No. of Five-Year Limited Convertible Term Policies in Force	44,915
No. of Permanent Plan Policies in Force	278,479
Face Value of Policies in Force	$2,988,386,321
Average Amount Per Policy in Force	$8,424
Average Attained Age in 1986	54.4 years
Average Annual Death Rate	6.9 per 1,000
Total Investments of VSLI Fund	$1,135,615,865
Average Rate of Return on All Investments (As of December 31, 1986)	9.27%
Total Disbursements in 1986	$125,356,320

SERVICE-DISABLED VETERANS' INSURANCE

(Policy Numbers Prefixed with "RH" or "ARH")

The Insurance Act of 1951 authorized the issuance of new insurance policies ("RH" prefix) to veterans separated from service on or after April 25, 1951, who are suffering from a service-connected disability but who are otherwise insurable. Coverage is available in amounts from $1,000 to $10,000 and, in general, must be applied for within one year from the date of the notice to the insured that he or she has been rated disabled by the Veterans Administration. Although information on SDVI is periodically released by our information services, eligible veterans are also sent notifications concerning possible entitlement. This is the only program of Government life insurance which is still open to new issues.

All plans of insurance are available unless the veteran is totally disabled at the time of application, in which case the endowment plans are not available.

Legislation was enacted in 1958 to protect those veterans who become incompetent from a service-connected disability while eligible to apply for SDVI, but who die before application is filed. Such veterans are deemed to have applied for $10,000 of insurance (less any existing Government life insurance), which is issued posthumously, and is payable to a preferred class of the insured's relatives in monthly installments. Since 1959, a total of $5,997,793 in gratuitous SDVI ("ARH" prefix) beneficiary payments have been made.

Since the SDVI program's inception in 1951, 304,429 policies have been issued, for a total of $2,786,556,900 of insurance coverage. We are currently issuing approximately 4,000 policies per year.

Program Statistics ("RH"):

Opening Date	April 25, 1951
Closing Date	Open
No. of Policies Issued	304,429
Face Value of Policies Issued	$2,786,556,900
Average Amount Per Policy Issued	$9,153
No. of Five-Year Term Policies in Force	82,937
No. of Permanent Plan Policies in Force	99,934
Face Value of Policies in Force	$1,658,270,782
Average Amount Per Policy in Force	$9,068
Average Attained Age in 1986	45.0 years
Average Annual Death Rate	12.8 per 1,000
Total Disbursements in 1986	$38,313,754
Percentage of Policies on Premium Waiver	23.3%

EXHIBIT A-4

VETERANS' REOPENED INSURANCE

(Policy Numbers Prefixed with "J", "JR" and "JS")

Program Summary:

In 1964, Congress enacted legislation which provided for a limited reopening of NSLI for a period of one year beginning May 1, 1965, to veterans (not on active duty at date of policy issue) who met the following conditions:

1. They must have been eligible to obtain NSLI between October 8, 1940, and January 1, 1957, and

2. They must have had either:

   a. A service-connected disability which was compensable, or would have been compensable if it were rated 10 percent or more in degree, without any serious nonservice-connected disability which would have disqualified them for standard insurance (prefixed with "J" or "JR"), or

   b. A nonservice-connected disability, or combination of service-connected and nonservice-connected disabilities, so serious that they could not obtain commercial insurance at the highest rates (prefixed with "JS").

All plans of insurance available under the NSLI program, except term insurance, are available under the Veterans' Reopened Insurance (VRI) program. Approximately 227,900 policies were issued under this program, of which 132,265 remain in force for a total of $860,827,100 of coverage.

Program Statistics:

Opening Date	May 1, 1965
Closing Date	May 2, 1966
No. of Policies Issued	227,882
Face Value of Policies Issued	$1,601,504,500
Average Amount Per Policy Issued	$7,028
No. of Policies in Force	132,265
Average Amount Per Policy in Force	$6,508
Face Value of Policies in Force	$860,827,100
Average Attained Age in 1986	63.7
Average Annual Death Rate	20.0 per 1,000
Total Investments of VRI Fund	$517,556,150
Average Rate of Return on All Investments (As of December 31, 1986)	9.77%
Total Disbursements in 1986	$113,986,058

EXHIBIT A-5

VA ADMINISTERED INSURANCE PROGRAMS

FACE AMOUNT OF COVERAGE - VA VERSUS COMMERCIAL INSURERS	EXHIBIT B-1
INVESTMENT FORMULA - INVESTMENTS PER PROGRAM	EXHIBIT B-2
PIE CHART - TRUST FUND INVESTMENTS	EXHIBIT B-3
CURRENT TREASURY YIELDS ON INVESTMENTS	EXHIBIT B-4
YIELD ON INVESTMENTS - NSLI VERSUS COMMERCIAL INSURERS	EXHIBIT B-5

EXHIBIT B

FACE AMOUNT OF COVERAGE – VA VERSUS COMMERCIAL INSURERS

(IN BILLIONS)

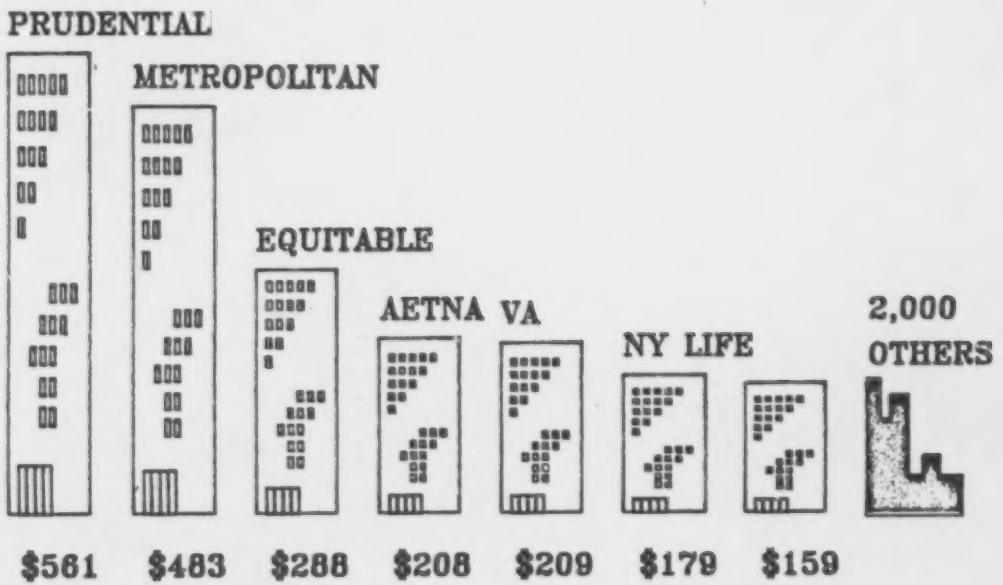


EXHIBIT B-1

INSURANCE TRUST FUND INVESTMENTS

June 30, 1987

U.S. Government Securities

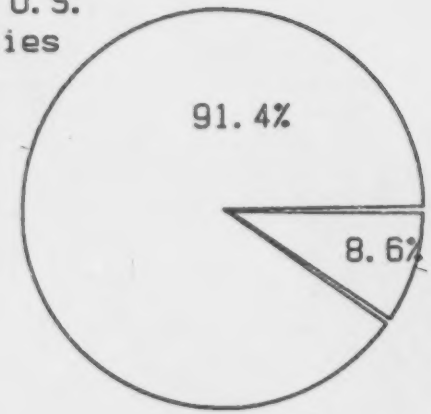
Fund	NSLI (V)	USGLI (K)	VSLI (RS/W)	VRI (J,JR,JS)
General Authority	38 U.S.C. 720(b)	38 U.S.C. 755(b)	38 U.S.C. 723(c)	38 U.S.C. 725(d)
Formula for Obtaining the Yield on U.S. Security Investments	The average market yield on all marketable interest-bearing obligations of the public debt of the U.S. that are not due or callable until after the expiration of 3 years. (Minus ⅛% for funds invested prior to January 1, 1985). Calculated as of the end of the preceding month.	The average market yield on all marketable interest-bearing obligations of the public debt of the U.S. that are not due or callable until after the expiration of 3 years. (Minus ⅛% for funds invested prior to January 1, 1985). Calculated as of the end of the preceding month.	The average rate of interest (coupon rate) borne by all marketable interest-bearing obligations of the U.S., forming a part of the public debt that are not due or callable until after at least 5 years from the date of original issue.	The average market yield on all marketable interest-bearing obligations of the public debt of the U.S. that are not due or callable until after the expiration of 4 years. Calculated as of the end of the preceding month.
Portfolio Arrangement	All new and roll-over investments are spread over periods of 1 to 15 years so that there are equal amounts of maturities each June 30 for all funds except "K." Because of cash flow requirements, the investments being made in the "K" fund are all with maturity dates of the next June 30th.			
Formula Established By	1985 Agreement between the VA and Treasury	1985 Agreement between the VA and Treasury	PL 85-896	PL 88-664
Amount Invested in U.S. Government Securities	$10,245,531,000	$230,982,000	$1,094,574,000	$486,424,000
Average Rate Of Return on all Investments in U.S. Securities	9.558%	7.375%	9.585%	10.025%
Interest Rate on New Investments in U.S. Securities (Apr., May, June)	8.493%	8.500%	10.376%	8.619%
		Policy Loans		
Amount Invested in Policy Loans	$941,730,892	$22,345,615	$74,130,573	$27,392,361
Percentage of Trust Fund Investments in Policy Loans	8.418%	8.821%	6.343%	5.351%
Average Rate of Return on Policy Loans	5.161%	4.336%	6.406%	6.746%
		Total Investments		
Amount	$11,187,261,892	$253,327,615	$1,168,704,573	$513,816,361
Rate of Return on all Investments (Loans and U.S. Securities	9.188%	7.107%	9.383%	9.850%

Insurance Trust Fund Investments

As Of December 31, 1986

U.S. Government Securities

Amount Invested in U.S. Government Securities
$11,869,825,000



Amount Invested In Policy Loans
$1,118,158,668

Total $12,987,983,668

EXHIBIT B-3

VARDIC - April, 1987

INVESTMENT IN U.S. GOVERNMENT SECURITIES AS OF JULY 31, 1987

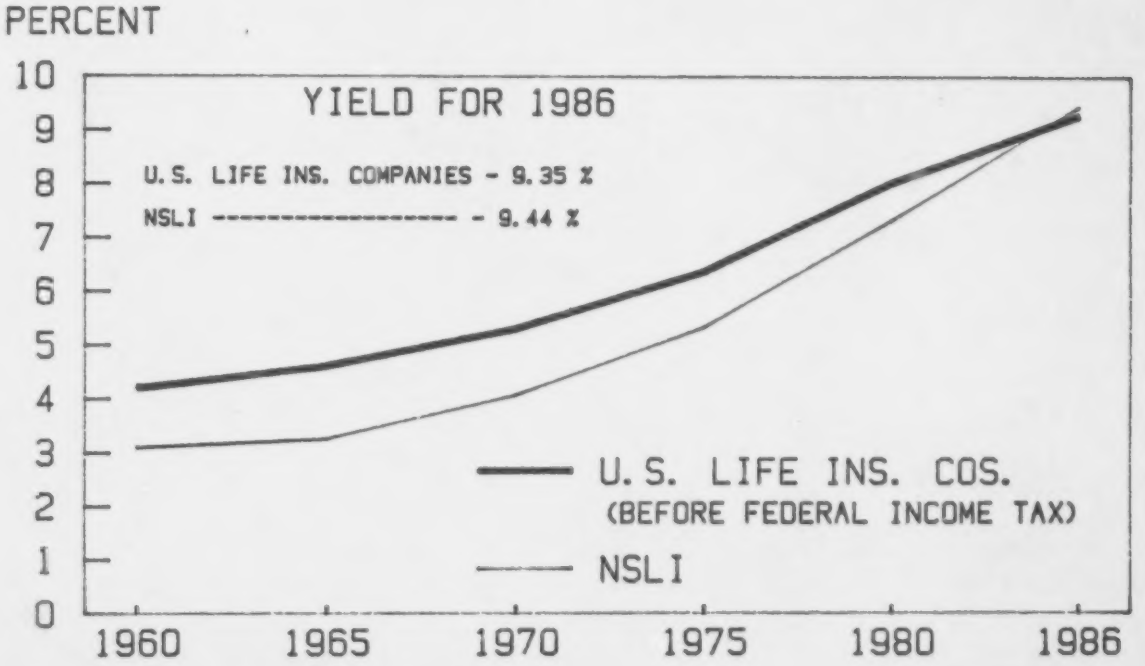
				Total Investment Par and Book Value
NATIONAL SERVICE LIFE INSURANCE FUND				
36X8132	Public Debt Securities	6-3/4%	1988 - 1992	$ 607,944,000
"	" " "	7%	1988 - 1990	326,623,000
"	" " "	7-1/4%	1988 - 1991	459,679,000
"	" " "	7-1/2%	1988 - 1989	142,910,000
"	" " "	8%	1988 - 1993	1,004,796,000
"	" " "	*8-3/8%	1988	25,971,000
"	" " "	8-1/2%	1988 - 2002	1,014,199,000
"	" " "	8-5/8%	1988 - 1994	815,984,000
"	" " "	9-1/2%	1988 - 1995	861,209,000
"	" " "	10-1/4%	1988 - 2000	909,429,000
"	" " "	10-1/2%	1988 - 1998	783,228,000
"	" " "	12-7/8%	1988 - 1996	640,770,000
"	" " "	13-1/8%	1988 - 1997	692,076,000
"	" " "	13-3/8%	1988 - 1999	845,794,000
		8-1/4%	1988 - 2001	949,086,000
36X8132	Participation Certificates	6.20%	Aug. 12, 1988	100,000,000
"	" " "	6.45%	April 8, 1988	35,000,000
				$10,214,698,000
VETERANS SPECIAL LIFE INSURANCE FUND				
36X8455	Public Debt Securities	5-7/8%	1988 - 1989	$ 17,813,000
"	" " "	6-3/8%	1988 - 1990	34,457,000
"	" " "	6-3/4%	1988 - 1991	45,873,000
"	" " "	7%	1988 - 1992	55,436,000
"	" " "	7-1/8%	1988 - 1993	64,810,000
"	" " "	7-1/2%	1988 - 1994	63,821,000
"	" " "	8-3/8%	1988 - 1995	69,219,000
"	" " "	9%	1988 - 1996	73,651,000
"	" " "	*10-3/8%	1988 - 1997	231,411,000
"	" " "	10-7/8%	1988 - 1998	94,518,000
"	" " "	11-1/8%	1988 - 2001	229,331,000
"	" " "	11-1/2%	1988 - 2000	115,332,000
				$1,095,672,000
UNITED STATES GOVERNMENT LIFE INSURANCE FUND				
36X8150	Public Debt Securities	6-1/2%	1988 - 1992	$ 36,999,000
"	" " "	6-3/4%	1988 - 1990	30,013,000
"	" " "	7%	1988 - 1991	34,096,000
"	" " "	7-1/4%	1988 - 1989	7,757,000
"	" " "	7-3/4%	1988 - 1993	85,207,000
"	" " "	*8-3/8%	1988	772,000
"	" " "	8-3/8%	1994	16,463,000
"	" " "	8-1/2%	1994 - 1995	17,167,000
				$ 228,474,000
VETERANS REOPENED INSURANCE FUND				
36X4010	Public Debt Securities	7-1/8%	1989 - 1992	$ 34,737,000
"	" " "	7-3/8%	1988 - 1990	24,520,000
"	" " "	7-1/2%	1988 - 1991	33,828,000
"	" " "	7-5/8%	1988 - 1989	14,992,000
"	" " "	8-1/4%	1988 - 1993	42,268,000
"	" " "	*8-1/2%	1988	3,876,000
"	" " "	8-5/8%	1988 - 2001	34,030,000
"	" " "	8-3/4%	1988 - 1994	45,169,000
"	" " "	9-3/4%	1988 - 1995	42,961,000
"	" " "	10-3/8%	2000	32,010,000
"	" " "	10-3/4%	1988 - 1998	47,730,000
"	" " "	13%	1988 - 1996	40,135,000
"	" " "	13-1/4%	1988 - 1997	43,129,000
"	" " "	13-3/4%	1988 - 1999	48,599,000
				$ 487,984,000
36X4009	Public Debt Securities	*8-1/2%	1988	57,000
36X4009	Public Debt Securities	8-5/8%	1988	146,012,000
				$ 146,069,000

*Indicates Interest Rate on Current month investments.

EXHIBIT B-4

YIELD ON INVESTMENTS

NSLI VS. COMMERCIAL LIFE INSURANCE COMPANIES



VARDIC Philadelphia, Pa. - July, 1987

INDIVIDUAL PROGRAM SUMMARIES

VA SUPERVISED GROUP INSURANCE PROGRAMS

SERVICEMEN'S GROUP LIFE INSURANCE	EXHIBIT C-1
VETERANS' GROUP LIFE INSURANCE	EXHIBIT C-2
VETERANS' MORTGAGE LIFE INSURANCE	EXHIBIT C-3

EXHIBIT C

SERVICEMEN'S GROUP LIFE INSURANCE

The Servicemen's Group Life Insurance (SGLI) program provides $50,000 life insurance coverage for individuals currently in the military service and for certain specified periods after separation or release from periods of reserve duty.

The program is supervised by the Veterans Administration but is administered by the Office of Servicemen's Group Life Insurance (OSGLI) under the terms as specified in a group insurance contract.

Full-time coverage is available for commissioned, warrant and enlisted members of the Army, Navy, Air Force, Marine Corps and Coast Guard; and commissioned members of the National Oceanic and Atmospheric Administration and the Public Health Service. Cadets or midshipmen of the four United States Service Academies are also provided full-time coverage.

Full-time coverage is also available to Ready Reservists who are scheduled to perform at least 12 periods of inactive training per year. Persons assigned to, or who upon application would be eligible for assignment to the Retired Reserve, and have not yet received their retirement pay and have not reached 61 years of age, are also eligible for full-time coverage.

Part-time coverage is provided to eligible members of the Reserves who do not quality for full-time coverage. Part-time coverage is in effect while such members are performing periods of active duty training.

At the present time, there are about 3.7 million members covered by the insurance.

The monthly premium rate for active duty members and Ready Reservists is $4.00 for $50,000 or 80 cents per $10,000 insurance if lesser amounts of insurance are elected. The premium rate for part-time coverage is $5.00 per year for $50,000 coverage.

Monthly premium rates for Retired Reservists for the maximum amount of coverage are: through age 39, $15.00; ages 40 through 49, $20.00; ages 50 through 59, $25.00.

The following statistical information is of interest:

Program Issue Date	September 29, 1965, to present for Active Duty Members May 24, 1974 to present for Ready and Retired Reserve Members
Number of Members Covered	3,477,000
Average Face Amount per Member	$49,709
Total Face Amount in Force	$172,837,000,000
Average Attained Age	28.4 years
Average Annual Death Rate	1.19 per year

EXHIBIT C-1

VETERANS' GROUP LIFE INSURANCE

Veterans' Group Life Insurance (VGLI) is a program of post-separation insurance which provides for the conversion of Servicemen's Group Life Insurance (SGLI) to a 5-year term policy at reasonable rates. This program, like SGLI, is supervised by the Veterans Administration but administered by the Office of Servicemen's Group Life Insurance (OSGLI).

At the end of the term period, a member has the right to convert the insurance to an individual commercial life insurance policy with any one of over 300 participating commercial insurance companies.

This insurance is not available to Retired Reservists. Eligible Retired Reservists who do not desire continued SGLI coverage may, however, elect to exercise the conversion privilege if they do so within a 120-day period following separation or release from reserve status.

Persons who are eligible to be covered are members being released from active duty for periods not specified as less than 31 days and Reservists who are performing training periods of less than 31 days who suffer an injury or disability which renders them uninsurable at standard premium rates.

Members of the Individual Ready Reserve (IRR) and Inactive National Guard (ING) are also eligible for VGLI coverage as of January 1, 1986. Application must be made to the OSGLI. Individuals who were members of the IRR and ING on January 1, 1986, have 120 days after that date to apply without evidence of good health. If application is not received during the 120 days, it may be made within a one-year period after the 120 days provided evidence of good health is submitted. Individuals being assigned to the IRR and ING after January 1, 1986, have 120 days after assignment to apply without evidence of good health and one year after that with evidence of good health. No applications will be accepted after one year and 120 days. At the end of the five-year term, as an alternative to the conversion privilege described above, members of the IRR or ING can renew their VGLI for an additional five-year term, so long as they remain in the IRR or ING. Application to renew the VGLI coverage must be received before it expires.

To apply for coverage, an eligible member must submit an application to the OSGLI with the required premium during the 120 days following separation or assignment to the IRR or ING. If a member fails to make application during this period, he or she may still do so for up to one year after SGLI coverage terminates, providing he or she submits evidence of insurability.

If a member is totally disabled at the time of separation from active duty and is granted extended free SGLI coverage, he or she may apply for the VGLI any time during the one year period of extension.

VGLI is issued in amounts of $10,000, $20,000, $30,000, $40,000 or $50,000, but not for more than the amount of SGLI the member had in force at the time of separation from active duty.

Effective for individuals separated from active duty or assigned to the IRR/ING on or after July 1, 1986, VGLI premiums have been restructured. The premiums for each age group have been set at a level which will cover the mortality expenses and administrative costs for that particular group.

The monthly premium rates for the maximum coverage amount are: through age 29, $6.00; ages 30-34, $10.00; ages 35-44, $17.00; ages 45-49, $21.00; ages 50-59, $26.00; and ages 60 and over, $37.50.

For individuals separated from active duty or assigned to the IRR/ING prior to July 1, 1986, the following monthly premium rates for the maximum coverage amount apply: through age 34, $8.50; and ages 35 and over, $17.00.

The following statistical information is of interest:

Program Issue Dates	August 1, 1974, to present
Number of Members Covered	241,344
Average Face Amount per Member	$36,039
Total Face Amount	$8,697,685,000
Average Attained Age	33
Average Annual Death Rate	2.98 per 1,000

EXHIBIT C-2

VETERANS' MORTGAGE LIFE INSURANCE

Veterans' Mortgage Life Insurance (VMLI) is designed to provide financial protection to cover an eligible veteran's outstanding home mortgage in the event of his or her death. The insurance is provided under a group policy issued to the Administrator of Veterans Affairs. The Office of Veterans' Mortgage Life Insurance, P. O. Box 81497, Lincoln, Nebraska 68501, has been established to administer the mortgage protection program under the supervision of the Veterans Administration.

The insurance is restricted to those disabled veterans who have received grants for the purpose of specially-adapted housing under the authority of title 38, United States Code, chapter 21. Such grants are available to those veterans who are entitled to compensation for service-connected permanent and total disability due to one or more of the following conditions:

1. Loss, or loss of use, of both legs, which precludes locomotion without the aid of braces, crutches, canes, or a wheelchair; or

2. Blindness in both eyes, having only light perception, plus the loss, or loss of use, of one leg; or

3. Loss, or loss of use, of one leg together with residuals of organic disease or injury which so affect the functions of balance or propulsion as to preclude locomotion without resort to a wheelchair.

4. Loss, or loss of use, of one lower extremity together with the loss, or loss of use, of one upper extremity, which so affect functions of balance or propulsion as to preclude, or render medically inadvisable, locomotion without specific aids.

Public Law 96-385, effective October 7, 1980, enlarged the class of veterans entitled to a housing grant under Chapter 21 of Title 38. It provides a grant of up to $5,000 for veterans (other than those eligible for assistance as described above) who are entitled to compensation for service-connected permanent and totally disability due to:

1. blindness in both eyes with 5/200 visual acuity or less, or

2. the anatomical loss of use of both hands.

The grant is for the purpose of acquiring adaptions needed for the eligible veteran's residence because of his or her disabilities.

The grant is conditioned upon residence in a home owned by the veteran or family member.

The lifetime maximum amount of VMLI allowed an eligible veteran may not exceed $40,000. The maximum amount is permanently reduced at the same time the principal of the mortgage loan is reduced below $40,000.

The maximum amount of insurance available at one time may not exceed the lesser of the following amounts:

1. $40,000

2. The reduced remaining coverage available if the veteran has already used a portion of his or her mortgage insurance protection on an earlier loan. This reduced maximum represents $40,000, less any amount paid on a prior loan of $40,000 or less.

3. The total mortgage loan if it is less than $40,000.

The insurance is not available to veterans who have reached their 70th birthday.

The insurance is payable at the death of the veteran only to the holder of the mortgage loan. No insurance is payable if the mortgage is paid off prior to the veteran's death.

If title of the mortgage property is shared with anyone other than the veteran's spouse, the insurance coverage is only for the percentage of the title that is in the veteran's name.

A veteran is automatically insured upon receipt of a grant and the securing of a mortgage on the property.

The premiums for this protection are based only on the mortality costs of insuring standard lives and should, therefore, be lower than any commercial insurance premiums for similar coverage.

The following statistical information is of interest:

Program Issue Dates	August 11, 1971, to present
Number of Members Covered	5,644
Average Face Amount per Member	$32,272
Total Face Amount in Force	$182,143,696
Average Annual Death Rate	38.22 per 1,000

SGLI (SERVICEMEN'S GROUP LIFE INSURANCE)

(ACTIVE DUTY; READY & PART-TIME RESERVISTS; 120-DAY POST-SEPARATEES)

STATEMENT OF OPERATIONS

(Accrual Basis)

INCOME	POLICY YEAR 1986	CUMULATIVE FROM SEPT. 29, 1965
SERVICE PERSONNEL PREMIUMS	$132,390,390	$2,245,121,355
EXTRA HAZARD PAYMENTS.	0	508,247,406
INTEREST EARNED.	39,325,400	273,883,913
TOTAL.	171,715,790	3,027,252,674
DISPOSITION OF INCOME		
DEATH CLAIMS	$169,351,642	$2,453,979,260
NET COST OF EXTRA MORTALITY ON CONVERSIONS.	-1,907,607	25,298,773
EXPENSES OF ADMINISTRATION	1,575,804	26,518,712
TAXES AND FEES	2,342,581	46,349,804
DEPOSIT OR ADJUSTMENT TO POST-SEPARATION INSURANCE SUBFUND	1,068,366	3,356,489
TRANSFER TO RETIRED RESERVES	9,111,754	55,328,684
TRANSFER TO VGLI	4,226,098	130,751,631
CONTINGENCY RESERVE.	-14,052,848	285,669,321*
TOTAL.	$171,715,790	$3,027,252,674

*$92,276,246 of the Contingency Reserve was deposited in the revolving fund established under title 38, United States Code, section 769(d)(1) in the Treasury of the United States, as a return of premiums. These funds have been invested by the Secretary of the Treasury in special interest-bearing obligations of the United States. As of September 30, 1986, the total amount in the revolving fund including interest was $133.7 million.

United States General Accounting Office

GAO

Report to the Congress

July 1987

FINANCIAL AUDIT

Veterans Administration's Financial Statements for Fiscal Year 1986

GAO/AFMD-87-38

GAO

United States
General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

B-226801

July 29, 1987

To the President of the Senate and the
Speaker of the House of Representatives

This report presents the results of our examination of the Veterans Administration's (VA) consolidated financial statements for the fiscal year ended September 30, 1986. Our report describes restrictions on the scope of our examination, the result of which was to limit our opinion to VA's consolidated statement of financial position as of September 30, 1986. The opinion is qualified for our concerns about the fair presentation of land, buildings, and equipment, and for our concerns that insurance reserves are not calculated in accordance with generally accepted accounting principles for federal agencies.

The report contains separate reports on VA's system of internal accounting controls and on its compliance with laws and regulations. VA's medical care programs have internal accounting control weaknesses affecting patients' billings. VA did not fully comply with provisions of the Prompt Payment Act (31 U.S.C. 3901-3906) and the debt collection provisions of the Veterans' Rehabilitation and Education Amendments of 1980 (38 U.S.C. 3115).

VA was established in July 1930 as an independent agency under the President by Executive Order 5398, in accordance with the act of July 3, 1930 (46 Stat. 1016). VA is responsible for administering federal benefit programs for veterans and their dependents. These programs include compensation payments for disabilities and death related to military service, as well as for pensions, education and rehabilitation, home loan guaranties, burial payments, comprehensive medical care, and life insurance.

We are sending copies of this report to the Director of the Office of Management and Budget; the Chairman and former Chairman, Senate Committee on Veterans' Affairs; the Chairman, House Committee on

Veterans' Affairs; the Secretary of the Treasury; and the Administrator of Veterans Affairs.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

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Abbreviations

DMS	Department of Medicine and Surgery
GAO	General Accounting Office
VA	Veterans Administration

GAO

United States
General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

B-226801

To the Administrator of Veterans Affairs,
Veterans Administration

We have examined the consolidated statement of financial position of the Veterans Administration (VA) as of September 30, 1986, and the related consolidated statements of operations and changes in financial position and reconciliation to budget for the fiscal year then ended. Our examination was made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances, except as indicated in the following two paragraphs.

For fiscal year 1985, VA did not prepare its financial reports nor maintain its accounting records in accordance with generally accepted accounting principles for federal agencies, which became effective in November 1984. Although VA adopted such principles as of the beginning of fiscal year 1986, it was not practicable to extend our auditing procedures to enable us to express an opinion on the accompanying consolidated statements of operations and changes in financial position and reconciliation to budget or on the consistency of application of accounting principles with the preceding year.

The consolidated statement of financial position includes land, buildings, and equipment, many of which were acquired by or transferred to VA over periods dating back to its establishment in 1930. Because these assets were acquired over periods dating back so many years, documents of original cost are no longer readily obtainable, and we were unable, by means of alternative auditing procedures, to satisfy ourselves as to the aggregate net book value of land, buildings, and equipment.

VA uses statutorily mandated investment yields and mortality rates to calculate its insurance reserves on its life insurance programs (note 5). Assumed investment yields used by VA have ranged from 2.25 percent to 4.50 percent and mortality rates used by VA were developed over periods dating back to 1936. The insurance reserve balance calculated under generally accepted accounting principles for federal agencies differs from that under statutory assumptions, since more current actuarial assumptions are used. Had the insurance reserves been calculated under generally accepted accounting principles for federal agencies, we have estimated that the insurance reserve balance of $11.2 billion would be lower by as much as $4.0 to $5.7 billion.

Note 3 to the consolidated financial statements contains amounts of future liabilities for VA's compensation and pension programs. These future liabilities have been disclosed to show the magnitude of the probable future costs VA will incur for benefits it is committed to pay under its compensation and pension programs. These amounts are estimates based on historical trends and statistics prevailing as of September 30, 1986. To the extent that economic and demographic factors which affect these trends change in the future, these liabilities will increase or decrease accordingly.

In our opinion, except for the effect on the consolidated statement of financial position of such adjustments as might have been necessary had we been able to perform the necessary auditing procedures to satisfy ourselves as to the net book value of land, buildings, and equipment and except for the effect on the insurance reserves that would have resulted had VA used actuarial assumptions based on generally accepted accounting principles for federal agencies, the accompanying consolidated statement of financial position presents fairly the financial position of the Veterans Administration at September 30, 1986, in conformity with generally accepted accounting principles for federal agencies.

Our examination was made for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The supplemental schedules included in note 10 are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. The supplemental schedules have been subjected to the auditing procedures applied in the examination of the basic consolidated financial statements. In our opinion, except for the effect on the schedule of assets, liabilities, and equity of the matters discussed in the preceding paragraph, the schedules of assets, liabilities, and equity and of budgeted and actual outlays by major program are fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole. For the reasons discussed in the second paragraph of this report, we do not express an opinion on the schedule of expenses, dividends, revenue, and financing sources by major program or on the schedule of sources and uses of resources and reconciliation to budget by major program.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

May 1, 1987

Report on Internal Accounting Controls

We have examined the consolidated financial statements of the Veterans Administration (VA) for the fiscal year ended September 30, 1986, and have issued our report thereon dated May 1, 1987. This report pertains only to our study and evaluation of the system of internal accounting controls for the fiscal year ended September 30, 1986.

As part of our examination, we made a study and evaluation of the system of internal accounting controls to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on VA's consolidated financial statements. For purposes of this report, we have classified the significant internal accounting controls in the following categories:

- medical care,
- life insurance,
- compensation and pension,
- housing credit assistance,
- education,
- construction,
- payroll,
- administration and other, and
- financial reporting.

Our study included all of the control categories listed above except for the administration and other and the financial reporting categories. For these activities, we found it more efficient to expand the scope of our substantive audit tests. In addition, we reviewed VA's report issued pursuant to section 2 of the Federal Managers' Financial Integrity Act of 1982 to identify and determine the status of internal control weaknesses relevant to financial matters.

VA's management is responsible for establishing and maintaining a system of internal accounting controls in accordance with the Accounting and Auditing Act of 1950 and the Federal Managers' Financial Integrity Act of 1982. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system of internal accounting controls are to provide management with reasonable assurance that (1) obligations and costs are in compliance with applicable laws, (2) funds, property, and other assets are safeguarded against waste, loss, and unauthorized use or misappropriation, and (3) assets,

liabilities, revenues, and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over agency assets. Because of inherent limitations in any system of internal accounting controls, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation, made for the limited purpose described in the second paragraph, would not necessarily disclose all weaknesses in the system. Accordingly, we do not express an opinion on VA's system of internal accounting controls taken as a whole or on the categories of controls identified in the second paragraph. However, our study and evaluation disclosed the following condition which we believe could result in errors or irregularities in amounts material in relation to VA's consolidated financial statements, which may not be promptly detected.

Billings Not Always Rendered for Medical Services

Internal accounting control procedures involving billings for medical services are not being followed at many of VA's medical centers. Thus, VA cannot be assured that all patients receiving medical care for which VA should be reimbursed are properly billed for these services.

VA can obtain reimbursement for some or all medical services provided to certain veterans depending on either their income level or their ability to defray costs. Effective July 1, 1986, 38 U.S.C. 610 established a "means test" for veterans with disabilities that did not result from military service whereby a veteran's ability to defray medical costs is determined based upon his or her income level. Those veterans that meet or exceed these income levels must agree to pay VA an established deductible ("copayment").

VA's Department of Medicine and Surgery policy manual requires that eligibility for treatment be determined and verified. Determination of eligibility is based on information furnished by the veteran on the application form. The information must then be verified. VA cannot delay providing medical care while verifying a veteran's eligibility or financial means. However, in order to ensure that VA will render billings for all reimbursable medical care, it is equally important that patients' eligibility status be determined and verified.

We found that documentation for determining patients' eligibility status was inadequate in many cases. Of the 1,225 cases reviewed at 43 of 172 hospitals, 160 did not have complete documentation for verifying the patients' eligibility status. Of these 160 cases, 31 patients' files did not contain the required VA Form 10-10F, "Financial Worksheet," which is used to gather and analyze financial data for those patients who are unable to defray medical care expenses. The remaining cases lacked the necessary evidence to show that the hospital verified the information included on the patients' application forms.

We also reviewed an additional 191 cases where patients receiving treatment should have been billed. Of these 191 cases, 34, or 18 percent, of the patients were not billed. The 34 cases where no billing was rendered involved patients not eligible for free treatment or patients who were required to pay VA a preestablished deductible (copayment) pursuant to 38 U.S.C. 610.

Patients who should be billed are receiving free treatment. In the past, the amount of potential revenue generated from these patients was minimal. As of September 30, 1986, VA's records showed about $20.2 million of receivables for ineligible hospitalization cases. With the new copayment requirements, however, the number of patients who should be billed for medical services is expected to increase significantly as is the anticipated revenue from such billings.

Conclusions and Recommendation

Stronger internal accounting controls are needed to maximize reimbursements and to ensure that all veterans who have received medical services for which VA should be reimbursed are identified and billed. Given the current constraints on federal budgetary resources, it is also important that VA obtain all reimbursements it is entitled to receive.

We recommend that the Administrator of Veterans Affairs direct the Department of Medicine and Surgery (DMS) to review the medical centers' compliance with VA's procedures for determining the eligibility status of veterans from whom reimbursements should be received. For those medical centers where compliance is not being achieved, DMS should provide the Administrator with a detailed plan of corrective actions.

Except for the above weaknesses and those identified by VA in its report pursuant to section 2 of the Federal Managers' Financial Integrity Act,

our study and evaluation disclosed no other conditions which we considered to be material in relation to the consolidated financial statements taken as a whole. We considered the above weaknesses in determining the nature, timing, and extent of our audit tests. We concluded that these weaknesses in internal accounting controls do not affect our opinion on the consolidated financial statements.

Other Opportunities for Improvement

During the course of our examination, we identified a number of weaknesses in internal accounting controls and procedures which we are reporting separately to the Administrator of Veterans Affairs. Although we did not consider these weaknesses to be material to the consolidated financial statements, they nonetheless merit corrective action to strengthen VA's internal accounting controls.

Agency Comments

Although we did not obtain formal comments on this report, we did provide appropriate VA officials with a draft of the report and agreed to incorporate their informal comments. The Director of Administration of DMS commented that "VA Medical Centers are currently using the Decentralized Hospital Computer Program (DHCP) to partially automate this billing process. It is hoped that within the next 2-3 years the billing process will be fully automated. Concurrently, DMS is also doing its utmost to automate its eligibility procedures through use of DHCP computers."

Report on Compliance With Laws and Regulations

We have examined the consolidated financial statements of the Veterans Administration (VA) for the fiscal year ended September 30, 1986, and have issued our report thereon dated May 1, 1987. Our examination was made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including tests of compliance with laws and regulations, as we considered necessary in the circumstances.

In our opinion, VA, except for the matters discussed below, complied with the terms and provisions of laws and regulations for the transactions tested that could have materially affected VA's consolidated financial statements.

Violations of the Prompt Payment Act

During fiscal year 1986, VA did not always pay to vendors the interest penalties that the Prompt Payment Act (31 U.S.C. 3901-3906) requires for late payments. However, VA has implemented an automated payment system to improve the timeliness of its payments to vendors.

The Prompt Payment Act provides governmentwide payment standards for determining when federal agencies should pay commercial vendors. Additionally, the act requires agencies, in the absence of contractual agreements stating otherwise, to pay interest penalties on amounts paid after prescribed grace periods.

VA has not complied fully with the requirements of the act. During fiscal year 1986, 17 percent of the agency's payments subject to the act were made after due dates (16 percent within the grace period and 1 percent requiring interest). VA paid approximately $586,000 in interest penalties on payments made after the specified grace period, but postpayment audits revealed that penalties were not paid, as required, in all instances.

VA has reported its Prompt Payment Act violations to the President in accordance with section 2 of the Federal Managers' Financial Integrity Act and to the Office of Management and Budget as required by the Prompt Payment Act (31 U.S.C. 3905).

In 1986, VA implemented an automated payment system which improved the timeliness of vendor payments. This system, the Computer Assisted Payment Processing System, automated the matching of vendor invoices with receiving reports and calculates interest on late payments. All VA facilities were fully converted to the system by August 1986, and VA

officials expect that the system will enable the agency to comply more fully with provisions of the Prompt Payment Act.

Violations of the Veterans' Rehabilitation and Education Amendments of 1980

The Veterans' Rehabilitation and Education Amendments of 1980 (Public Law 96-466, now codified at 38 U.S.C. 3115) specifies interest and administrative costs to be charged to VA's delinquent debtors. This law requires that interest on delinquent debt should be accrued based on the Department of the Treasury's rate, which, as of September 30, 1986, was 8 percent. However, during fiscal year 1986, VA did not fully comply with the provisions of the Veterans' Rehabilitation and Education Amendments of 1980 because it did not assess interest and administrative costs on certain debts generated by its compensation and pension program. These debts principally relate to overpayments of compensation and pension benefits for which VA is seeking reimbursement. Section 3102 of title 38 of the United States Code allows VA to waive interest and administrative costs if assessment is deemed to be against equity and good conscience. However, to date, no waivers have been executed. We also noted that VA used an interest rate of 4 percent—below the rate required by the Veterans' Rehabilitation and Education Amendments of 1980—to assess interest on delinquent loan guaranty debts.

Applicability of the Debt Collection Act of 1982 to VA

There is an unresolved issue as to whether VA should also be accruing penalties on its delinquent debt as required by section 11 of the Debt Collection Act of 1982 (Public Law 97-365, now codified at 31 U.S.C. 3717). VA maintains that it is not subject to the penalty provisions of the Debt Collection Act because the Veterans' Rehabilitation and Education Amendments of 1980, which predates the former act by 2 years, fixes interest and charges applicable to debts owed VA but provides no specific authority for assessment of penalties. In our previous report Debt Collection: Billions Are Owed While Collection and Accounting Problems Are Unresolved (GAO/AFMD-86-39, May 23, 1986), we stated that because the Debt Collection Act was intended to improve governmentwide collection efforts and because the VA-specific legislation does not address penalties, an argument can be made that VA should assess penalties on its delinquent debt in accordance with the Debt Collection Act. VA submitted a request for a Comptroller General decision regarding this question, and, as of this date, our decision is pending.

Treatment of October 1, 1986, Entitlement Payments

VA terminated processing benefit entitlements under its compensation and benefit programs late in fiscal year 1986. The payments for these entitlements were made as scheduled on October 1, 1986. The use of fiscal year 1987 funds to pay obligations which normally would have been processed and paid out of funds available for use in fiscal year 1986 raised a question, which arose late in our audit, whether the later enacted fiscal year 1987 appropriation was available for those payments. We are examining these issues and will address them separately.

Conclusions and Recommendation

VA has made progress in complying with the Prompt Payment Act, but it should continue to monitor late payments to ensure that all penalties are paid as required.

VA is not fully complying with the provisions of the Veterans' Rehabilitation and Education Amendments of 1980. We recommend that the Administrator of Veterans Affairs conduct a review of VA's delinquent debts and, accordingly, either assess the proper amount of interest and administrative costs, as required by law, or execute waivers if there are appropriate reasons for doing so.

In connection with our examination, except for the matters discussed above, nothing came to our attention that caused us to believe that VA was not in compliance with the terms and provisions of laws and regulations for those transactions not tested.

The matters explained above were considered in determining the nature, timing, and extent of the audit tests to be applied in our examination, and they do not affect our opinion on VA's consolidated financial statements dated May 1, 1987.

Agency Comments

Although we did not obtain formal comments on this report, we did provide appropriate VA officials with a draft of the report and agreed to incorporate the agency's comments. The Department of Veterans Benefits Debt Management Staff Director commented that "With limited ADP resources, priority emphasis has been placed on debt collection initiatives such as IRS income tax refund offset. Our ADP modernization plans will address compliance with all provisions of the Veterans' Rehabilitation and Education Amendments of 1980." VA's Director, Office of Program Analysis and Evaluation, commented, "Once the report has been issued formally, we will track progress made toward implementing the GAO recommendations as part of the quarterly program performance

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review process. We will also continue to monitor VA's efforts to comply with the provisions of the Prompt Payment Act and the Debt Collection Act through the internal control segment of the performance review process."

Financial Statements

Consolidated Statement of Financial Position

VETERANS ADMINISTRATION

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
SEPTEMBER 30, 1986

(Dollars in Thousands)

ASSETS:	
Fund Balance with U. S. Treasury	$ 6,148,403
Imprest Funds	9,790
Advances, Accounts, and Loans Receivable, net (note 7)	3,404,365
Investments (note 6)	11,789,489
Foreclosed Property Held for Sale	807,531
Land, Buildings, and Equipment Net of Accumulated Depreciation (note 8)	6,310,049
Other Assets	154,585
Future Financing Sources	2,160,312
TOTAL ASSETS	$ 30,784,524
LIABILITIES AND EQUITY:	
Accounts Payable, Principally to the Public	$ 1,041,710
Accrued Compensation and Pension Benefits	1,259,671
Accrued Payroll and Payroll Related Liabilities	846,912
Dividends on Credit or Deposit (note 5)	630,381
Insurance Dividends Payable (note 5)	929,714
Other Liabilities	382,386
Reserve for Losses on Guaranteed Loans (note 4)	1,735,252
Insurance Reserves (note 5)	11,229,292
Borrowings from Treasury	1,730,078
TOTAL LIABILITIES	19,785,396
EQUITY OF THE U.S. GOVERNMENT:	
Unrealized Appropriations:	
Deferred Appropriations	6,612,935
Unobligated Balances	2,146,143
Undelivered Orders	1,518,269
Trust Fund Balances	669,502
Insurance Fund Balances	52,279
TOTAL EQUITY OF THE U.S. GOVERNMENT	10,999,128
TOTAL LIABILITIES AND EQUITY	$ 30,784,524

The accompanying notes are an integral part of these statements.
Note 10 includes financial information by major program area.

Consolidated Statement of Operations

VETERANS ADMINISTRATION

CONSOLIDATED STATEMENT OF OPERATIONS
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986

(Dollars in Thousands)

OPERATING EXPENSES AND DIVIDENDS:	
Expenses by Category:	
Personnel Compensation and Fringe Benefits	$ 6,582,472
Veterans Benefits	19,695,819
Insurance Claims and Indemnities	1,112,657
Depreciation	337,997
Supplies and Materials	1,537,771
Contractual Services	1,180,408
Rent, Communications, and Utilities	503,446
Other	1,429,705
Total Operating Expenses	28,380,275
Dividends to Insurance Policyholders (note E)	908,251
	$29,288,526
OPERATING REVENUE AND FINANCING SOURCES:	
Operating Revenues:	
Premium Income	$ 845,559
Interest Income	1,350,391
Loan Origination fees	258,111
Reimbursements and Other	377,142
Total Operating Revenue	2,831,203
Financing by Source:	
Appropriations Realized	26,230,260
Transfers, Reimbursements, and Other	227,063
Total Financing Sources	26,457,323
	$29,288,526

The accompanying notes are an integral part of this statement.
Note 10 includes financial information by major program area.

Consolidated Statement of Changes in Financial Position and Reconciliation to Budget

VETERANS ADMINISTRATION

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION AND RECONCILIATION TO BUDGET
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986

(Dollars in Thousands)

NET USE OF RESOURCES:	
Operations:	
Operating Expenses	$ 28,380,275
Items Requiring (Providing) Funds:	
Increase in Insurance and Guaranteed Loan Reserves	(695,096)
Depreciation	(337,997)
Increase in Accounts Receivable	60,821
Increase in Accounts Payable and Accruals	(174,165)
Revenues Accounted for as	
Offsetting Collections	(2,114,310)
Funds Used By Operations	25,119,328
Non-Operating Uses:	
Dividends (note 5)	925,149
Acquisitions of Land, Buildings and Equipment	952,690
Purchase of Foreclosed Property Held for Sale	1,147,210
Issuance and Repurchase of Loans and Liens	1,085,081
Other, Net	34,083
Financing Activities:	
Sale of Foreclosed Property Held for Sale	(1,214,867)
Sale of Loans, with Recourse	(818,368)
Loan and Lien Repayments	(284,809)
Disposals of Equipment and Other	(296,534)
Revenues Collected for Treasury	(113,253)
NET USE OF RESOURCES (BUDGETARY OUTLAYS)	26,535,710
RESOURCES PROVIDED:	
Current Year Appropriation	26,464,426
Less: Reductions Pursuant to P.L. 99-177 (Gramm-Rudman-Hollings)	(234,053)
Current Year Appropriations, Net	26,230,373
Interest on Government Securities	943,956
Net Transfers, Reimbursements and Other	(95,185)
Funds Returned to Treasury	(58,723)
TOTAL RESOURCES PROVIDED	27,020,421
INCREASE IN U.S. TREASURY AND IMPREST FUNDS	484,711
Funds Exchanged for U.S. Government Securities	(360,611)
NET INCREASE IN U.S. TREASURY AND IMPREST FUNDS	124,100
U.S. TREASURY AND IMPREST FUNDS:	
Beginning of Year	6,034,093
End of Year	$ 6,158,193

The accompanying notes are an integral part of this statement.
Note 10 includes financial information by major program area.

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Notes to the Financial Statements

NOTE 1: ACCOUNTING POLICIES

Entity and Basis of Consolidation

In fulfilling its mission to provide veterans with care, support and recognition, the Veterans Administration maintains 15 general funds, 10 revolving funds, 5 trust funds and 10 other funds. The financial activities of these funds have been classified into the following functional areas: medical and construction; compensation, pension, education and other benefits (veterans benefits); housing credit assistance; life insurance; and administration. Some of the trust and revolving fund activities for the insurance and housing credit assistance programs are augmented by budget appropriations.

The consolidated financial statements account for all funds for which the VA is responsible and are presented on the accrual basis of accounting as required by the GAO policy and procedures manual for guidance of Federal agencies (Title 2). All significant intra-agency balances and transactions have been eliminated in consolidation.

Recognition of Financing Sources

Financing sources are provided through Congressional appropriations on both an annual and multi-year basis. They may be used to fund operating expenses as well as capital expenditures such as for land, buildings, equipment and other long term assets as specified by law.

The current budgetary process does not distinguish between capital and operating expenditures. For budgetary purposes, both are recognized as a use of budgetary resources (outlays) as paid.

For financial reporting purposes under accrual accounting, however, operating expenses are recognized currently while expenditures for capital and other long term assets are capitalized and are not recognized as expenses until they are consumed in the VA's operations. Financing sources for these expenses, which derive both from current and prior year appropriations, are recognized on this same basis.

To the extent current or prior year appropriations are not available to fund certain accrued expenses, such as for annual leave earned but untaken and for losses on guaranteed loans, funding will be obtained from future financing sources. Accordingly, a financing source has been recognized for those expenses that will be paid from future financing sources.

Operating Revenue Recognition

Insurance premiums are recognized as revenue when due. Loan origination fees, which are charged to veterans at a rate of 1% of the loan principal, are recognized as revenues at the time of the guaranty.

Funds With U.S. Treasury

Funds with U.S. Treasury consist of all unexpended balances on the VA's accounts with the U.S. Treasury. As of September 30, 1986, $1,518,269,000 represents funds available to pay outstanding obligations while the remaining balance is available until expended.

Accrued Compensation and Pension Benefits

Compensation and pension benefits are accrued when veterans have satisfied the VA's eligibility criteria. This accrual only pertains to benefits due and payable in a particular fiscal year. See note 3 for a description of the VA's future liability under its compensation and pension program.

Losses on Guaranteed Loans

Upon foreclosure of a guaranteed loan, the VA may be required to pay the maximum claim, acquire the property, or acquire the property and pay less than the maximum claim pursuant to criteria established in Section 1816 of Title 38, United States Code. Thus, when the VA acquires the property, the cost is comprised of the

claimed amount paid the lender less net proceeds from the sale of the property. The VA incurs an additional cost for direct home (vendee) loans, issued upon the sale of foreclosed property, that subsequently default.

Estimated losses on anticipated defaults of guaranteed loans are recorded as expenses and a reserve is established at the time loans are guaranteed. This reserve represents the estimated cost of defaults for those guaranteed loans which will, based on prior default experience, default in the future. A portion of this reserve is subsequently reclassified as a reduction to direct home loans receivable when such loans are issued (see note 7) and as a reduction of foreclosed property held for sale when property is acquired, in order to record such property at its net realizable value.

Insurance Program Liabilities

Insurance program liabilities are recorded for unpaid claims in process, for an experience based estimate of claims incurred but not reported, and for incurred death and permanent disability installment claims. These liabilities are included in accounts payable.

Insurance Cash Surrender Value

All whole life policies build cash surrender values equal to the policy reserve plus any dividends held on account. Policy holders may borrow up to 94% of the cash surrender value or use it to purchase paidup insurance.

Annual, Sick and Other Leave

Annual leave is accrued as earned and is relieved as leave is taken. Sick and other types of leave are expensed as taken.

Dividends Payable

Dividends from the VA's insurance programs are recorded as a liability and are relieved either from operations or from the insurance fund balance when declared by the Administrator of Veterans Affairs. Dividends are normally declared when fund balances are in excess of statutorily required insurance claim reserves. Prior to Fiscal Year 1986 VA recorded dividends as an expense when paid.

NOTE 2: INTRAGOVERNMENTAL FINANCIAL ACTIVITIES

The VA's financial activities interact with and are dependent upon those of the Federal Government as a whole. Thus, VA's financial statements do not reflect the results of all financial decisions and activities applicable to it, as if it were a stand-alone entity.

- The VA's consolidated financial statements are not intended to report the Agency's proportionate share of the Federal deficit or of public borrowings, including interest thereon. Financing for budget appropriations reported on the VA's statement of operations could derive from tax revenues or public borrowings or both; the ultimate source of this financing, whether it be tax revenues or public borrowings, has not been specifically allocated to the VA.
- Financing for major and minor construction projects was obtained through budget appropriations. To the extent this financing was derived from public borrowings, no interest has been capitalized since such borrowings are recorded in total by the Department of the Treasury and are not allocated to individual departments and agencies.
- During Fiscal Year 1986 the majority of the VA's employees participated in the contributory Civil Service Retirement System (CSRS), to which VA made matching contributions. Such contributions amounted to $352,630,000 for fiscal year 1986. The VA does not, however, report CSRS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to its employees since this data is only reported in total by the Office of Personnel Management.

On January 1, 1987 the new Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. Employees hired after December 31, 1983 are automatically covered by FERS while employees hired prior thereto may elect to either join FERS or remain in CSRS. One of the primary differences between FERS and CSRS is that FERS offers a savings plan to which VA will automatically contribute 1% of pay and then match employee contribution up to an additional 4% of their basic pay.

- Most legal actions that affect the VA and involve an amount in excess of $2,500 fall under the Federal Tort Claims Act and are paid from Treasury's Claims, Judgments and Relief Acts Fund. Thus, most contingent liabilities arising from legal actions originating at the VA will not affect its operations or financial condition.

- VA's Housing Credit Assistance program has a liability to the U.S. Treasury of $1.7 billion. These funds were originally provided to support the direct loan fund, but were subsequently transferred to the loan guaranty fund and have since been fully used. The liability bears no interest and VA's ability to pay it is contingent upon receiving other financing.

NOTE 3: FUTURE LIABILITY FOR COMPENSATION AND PENSIONS

Veterans or their dependants receive compensation benefits if the veteran was disabled or died from military service connected causes. War veterans or their dependents receive pension benefits if the veteran was disabled or died from non-service connected causes or is age 65 or older. Certain pension benefits are subject to specific income limitations. For Fiscal Year 1986, compensation and pension benefits were $10,427,024,000 and $3,850,179,000, respectively.

The VA has a future liability for benefits expected to be paid in future fiscal years to veterans and, if applicable, their survivors who have met or are expected to meet defined eligibility criteria. The future liability of the compensation and pension programs is not currently funded, nor is there any intent to do so. Rather, payments for benefits that become due in a particular fiscal year are financed from that year's appropriation; in effect on a pay as you go basis. Payments of the future liability as it becomes due rely on Congressional authorization of future tax revenues or other methods, such as public borrowings, for their financing.

The future liability for compensation and pension benefits represents the present value, using a 9.2% discount rate, of projected annual benefit payments. Projected benefit payments were based on assumed cost of living increases ranging from 1.3% to 3.6% for 1987 - 1991 and 5.0% to 5.7% thereafter. In addition, the mortality and accession rates used were based on trends in the current veteran population.

This calculation was not based on an independent actuarial study and thus there is a risk that the assumptions and methods underlying it may not be reflective of actual economic and demographic trends affecting veterans.

The present value of the estimated future liability for compensation and pension benefits payable for the next five fiscal years and thereafter is as follows (dollars in thousands):

1987	$ 13,117,307
1988	12,154,107
1989	11,326,699
1990	10,560,100
1991	9,817,609
Thereafter	95,356,660
TOTAL	$152,332,482

No liability for compensation and pension benefits has been included in the accompanying consolidated statement of financial position.

NOTE 4: HOUSING CREDIT ASSISTANCE PROGRAM - COST OF GUARANTEED LOAN DEFAULTS

Most of the VA's housing credit assistance program involves the partial guaranty of loans, primarily home mortgages, issued to eligible veterans by private lenders. The total amount of such loans at September 30, 1986 was $143 billion of which VA had guaranteed $63 billion. This guaranty in effect transfers some or all risk of default from the lender to the VA. The guaranty also provides other benefits to the veteran by inducing lenders to provide interest rates which are usually lower than conventional mortgage rates and by not requiring a down payment. Thus a subsidy is provided to veterans inasmuch as they are receiving terms that are more favorable than would exist without Federal Government involvement.

One element of this subsidy is the present value of the cost the VA will bear as loans already guaranteed default in the future. A reserve for estimated losses from such defaults has been included in the consolidated statement of financial position. The calculation of the present value of the cost of defaults is based on historical default data developed by the VA and assumes that guaranteed loans will default over a nine year period, as follows (dollars in thousands):

1987	$ 605,243
1988	487,274
1989	326,138
1990	254,884
1991	138,261
1992 - 1995	113,959
	$1,925,759

The projected cost of guaranteed loan defaults will not necessarily reflect the VA's future appropriation requests over the next nine years, since those requests will also include anticipated inflows and outflows of resources for non-operating uses such as for transfers, purchases and sales of property, and issuances and repayments of loans.

Of the total reserve of $1,925,759,000 recorded at September 30, 1986, $107,056,000 is offset against loans receivable (note 7) and $83,451,000 is offset against foreclosed property held for sale; the remainder is recorded as a reserve for losses on guaranteed loans on the consolidated statement of financial position.

To the extent revolving fund revenues are not sufficient to fund this future cost, then financing will have to be obtained from future appropriations or other Congressionally approved sources.

During Fiscal Year 1986 VA sold certain of its direct home mortgage loans to the public under agreements with recourse provisions for $88,368,000. Under these agreements, loans sold that subsequently default are repurchased by the VA. Any losses from defaults of repurchased loans are borne by the VA. Estimated losses from future defaults of loans sold with recourse are a component of the reserve for losses on guaranteed loans.

Commencing in Fiscal Year 1987, the VA will sell certain of its direct home mortgages to the public without recourse. Anticipated losses from defaults of these loans will be reflected in the reduced proceeds the VA will receive since, once they are sold, the VA is no longer liable for any such losses. Preparations for the sale of loans without recourse provisions, which will include some of the direct loans on hand as of September 30, 1986, have just recently begun and at present the VA is not able to determine the magnitude of the discount.

NOTE 5: LIFE INSURANCE PROGRAMS

The Veterans Administration administers the following six life insurance programs: National Service Life Insurance (NSLI); United States Government Life Insurance (USGLI); Veterans Special Life Insurance (VSLI); Service Disabled Veterans Insurance (SDVI); Veterans Reopened Insurance (VRI); and insurance policies funded through the Veterans Insurance and Indemnities (VII) account. SDVI is the only program still authorized to issue new insurance policies.

Data on insurance in force for each of these programs is as follows:

Program	Insurance in Force: Number of Policies	Insurance in Force: Amount (millions)	Principal Veterans Group Covered
NSLI	3,007,746	$21,679	WW II
USGLI	58,144	223	WW I
VSLI	357,148	3,162	KOREA/VIETNAM
SDVI	183,953	1,668	KOREA/VIETNAM
VRI	132,862	908	WW II/KOREA
VII	2,946	16	MISC.
Total	3,742,799	$27,656	

Insurance Reserves

Insurance reserves consist of the actuarial computation of the present value of amounts that will be necessary to pay benefits in the future as policyholders or their beneficiaries make benefit claims. The two most important factors used by the actuaries to compute these reserves are assumed investment yields and mortality rates. The assumed investment yields and mortality rates used by the VA are prescribed by Federal Statutes.

The statutory Insurance Reserve Balance as of September 30, 1986 consists of reserves for:

	Death Benefits	Death Benefit Annuities	Disability Income and Waiver of Premium	Other	Total
			(dollars in thousands)		
NSLI	$ 7,832,313	$ 498,662	$ 929,186	$ 129,719	$ 9,389,880
USGLI	181,837	35,728	2,798	1,371	221,734
VSLI	792,724	3,420	121,572	10,600	928,316
SDVI	248,075	2,341			250,416
VRI	407,153	1,219	29,363		437,735
VII	1,211				1,211
TOTAL	$ 9,463,313	$ 541,370	$1,082,919	$ 141,690	$11,229,292

These statutorily computed reserve balances differ from those that would have been computed under generally accepted accounting principles for federal agencies since more current investment yield and mortality experience assumptions would have been used. These more current assumptions are principally based on the following differences from VA's statutory assumptions:

- VA's statutes mandate interest yields ranging from 2.25% to 4.50%. Actual investment yields have ranged from 7.08% to 9.94% over the past 5 years.
- Statutory mortality rate assumptions include the American Experience Table and others dating back to 1936. More recent insurance mortality studies show longer life expectancies.

The statutory accounting principles used by the VA are the same as those used by many mutual life insurance companies in the United States.

Policy Dividends

The VA Administrator annually determines the excess funds available for dividend payment. Dividends to be paid are based on an actuarial analysis of the appropriate programs as of the end of the preceding calendar year. In addition

to regular annual dividends, the VA declared termination dividends of approximately $800,000 for VRI. These termination dividends represent a return of excess funds in insurance reserves. Dividends are declared on a calendar year basis and are paid on policy anniversary dates. Policyholders may receive them in cash, use them to pay premiums in advance, repay loans, purchase paid up insurance, or place them in an interest-bearing account. Dividends held to pay premiums in advance and those placed in interest-bearing accounts are recorded as dividends on credit or deposit on the consolidated statement of financial position. Dividends paid during Fiscal Year 1986 and accrued as of September 30, 1986 are as follows:

	NSLI	USGLI	VSLI	VRI	TOTAL
	(dollars in thousands)				
Paid	$ 764,086	$ 14,667	$ 69,018	$ 35,164	$882,935
Declared and Accrued	802,800	13,466	76,223	32,660	925,149

Of the $925,149,000 dividends declared and accrued for fiscal year 1986, $908,251,000 were provided from operations, while the remaining $16,898,000 were provided from the trust fund balance.

VA Supervised Insurance Programs

VA also supervises the administration of the Servicemen's Group Life Insurance Program (SGLI). While this program is supervised by VA, it is administered by the Prudential Insurance Company which provides group life insurance coverage and pays all claims and expenses associated with the program. This coverage is provided to members of the Military Services, to cadets attending service academies, and to active members of the Armed Forces Reserves, National Guard and ROTC performing certain activities.

VA's responsibilities are to act as the transfer agent for premiums paid by payroll deductions and for extra hazard costs paid by the service organizations involved. VA also determines the adequacy of SGLI's insurance reserves, and, if excess reserves exist, VA can both lower premium rates and withdraw excess funds. To date, VA has withdrawn approximately $93 million from these reserves. These funds, together with investment interest earned thereon, are held in a trust which, as of September 30, 1986, had a balance of $133.2 million. They remain available to augment Prudential's primary policy resources. SGLI's insurance in force at September 30, 1986 was $172 billion on 3,457,300 policies. In addition to SGLI, VA supervises a similar program, the Veterans Group Life Insurance Program, which insures 240,400 veterans and had insurance in force of approximately $8.2 billion at September 30, 1986.

NOTE 6: INVESTMENTS

Insurance program investments, which comprise most of VA's investments, are in non-marketable U.S. Treasury special bonds and certificates and, to a lesser degree, in GNMA participation certificates. Interest rates for Treasury Special securities are based on average market yields for similar Treasury issues. The special bonds, which mature during various years through 2001, are generally held to maturity unless needed to finance insurance claims and dividends. The certificates are short term in nature and are either redeemed or replaced at maturity depending upon the cash needs of the insurance program. At September 30, 1986 investment securities consist of:

Security	Interest Range	Insurance Programs	Other Programs	Total
		(dollars in thousands)		
Special Bonds	5.875-13.75%	$11,285,674		$11,285,674
Certificates	7.125-11%	214,344		214,344
GNMA Certificates	6.2-6.45%	135,000		135,000
Bonds	7.875-8.5%		$ 2,251	2,251
Notes	7-14.625%		17,420	17,420
Other	Various		134,800	134,800
		$11,635,018	$154,471	$11,789,489

All investments are in securities issued by the U.S. Department of Treasury except for GNMA, which were issued by the Government National Mortgage Association, a subdivision of the U.S. Department of Housing and Urban Development.

NOTE 7: RECEIVABLES

	ACCOUNTS	ADVANCES	LOANS	TOTAL
		(dollars in thousands)		
Current:				
Individuals/Corporations	$1,990,669	$ 56,550	$ 536,287	$2,583,505
Federal government	330,088	132,837		462,925
	2,320,756	189,387	536,287	3,046,430
Non-Current:				
Individuals/Corporations	42,364		1,968,101	2,010,465
Federal government	445			445
	42,809		1,968,101	2,010,910
Total Receivables	2,363,565	189,387	2,504,388	5,057,340
Allowance for doubtful accounts and loans	(1,545,919)		(107,056)	(1,652,975)
Net Receivables	$ 817,646	$ 189,387	$2,397,332	$3,404,365

Non-Federal accounts receivable principally represent amounts due from individuals for Education Loan defaults, Home Loan Guaranty and Direct Loan defaults, and Compensation and Pension overpayments. Federal accounts receivable are mostly accrued interest payments due from the U.S. Treasury Department on VA investments. Non-Federal advance payments are principally advances to VA construction contractors, grant recipients, beneficiaries and VA employees engaged in official travel. Federal advance payments are mostly to the General Services Administration for the procurement of supplies and equipment. Current loans receivable are wholly amounts due under VA's Housing Credit Assistance Program. Non-Current loans receivable represent amounts due from loans and liens against VA-issued life insurance policies and also amounts owed VA's Housing Credit Assistance Program beyond the next twelve months.

NOTE 8: PROPERTY AND EQUIPMENT

The majority of the reported property represents facilities and equipment used to provide medical care to veterans. Property and equipment, including transfers from other Federal agencies, are valued at cost. Expenditures for major additions, replacements and alterations are capitalized. Routine maintenance is recognized as an expense when incurred. Costs of construction are capitalized as Construction in Progress until completed and then transferred to the appropriate property account.

Buildings are depreciated using the straight line method over estimated useful lives ranging from 25 to 40 years, based upon the American Hospital Association's estimate of useful lives of hospital assets. Equipment is depreciated using the straight line method over useful lives, which, for most equipment, range from 5 to 20 years.

Property and equipment consisted of the following as of September 30, 1986:

	Cost	Accumulated Depreciation	Net Book Value
		(dollars in thousands)	
Land	$ 81,416	$	$ 81,416
Buildings	4,873,656	1,638,255	3,235,401
Equipment	2,543,943	1,433,636	1,110,307
Other	663,542	263,617	399,925
Construction in Progress	1,483,000		1,483,000
TOTAL	$9,645,557	$3,335,508	$6,310,049

Prior to 1986, VA did not record depreciation for property and equipment, except for equipment in its Supply Fund. During 1986, in addition to recording 1986 depreciation, VA also recorded accumulated depreciation of $2,982,024,000 relating to fiscal years prior to 1986. This amount has been treated as a prior period adjustment and the deferred appropriations account has been adjusted accordingly. Current year depreciation amounted to $337,997,000.

VA leases facilities, primarily office space and medical facilities, from GSA. These leases are cancelable without penalty. In addition, VA has operating leases with the public for office, data processing and other equipment. Fiscal Year 1986 rent expense for these leases amounted to approximately $77,628,000 from GSA and $27,577,000 from the public.

NOTE 9: COMMITMENTS AND CONTINGENCIES

VA is committed under obligations it has incurred as of September 30, 1986 for goods and services which have been ordered but not yet received (undelivered orders). Aggregate undelivered orders amounted to $1,518,789,000 at September 30, 1986. Of this amount, $755,962,000 relates to construction projects of both long and short term duration. The remainder is principally comprised of obligations for medical supplies and equipment which were incurred by VA in the normal course of fulfilling its mission.

VA is a party in various administrative proceedings, legal actions and claims brought by or against it. These primarily relate to allegations of medical malpractice but also include other tort claims and contract disputes. Under the Federal Tort Claims Act, any award, compromise or settlement in excess of $2,500 is paid from the Claims, Judgments and Relief Acts fund maintained by the Department of the Treasury, while those of $2,500 or less are paid by VA. Payments during Fiscal Year 1986 for awards, compromises and settlements resulting from such legal actions amounted to $33,410,000 from Treasury's Claims, Judgments and Relief Acts Fund and $256,806 from VA.

In the opinion of VA's management and general counsel, the ultimate resolution of legal actions still pending will not materially affect VA's operations or financial position.

NOTE 10: SUPPLEMENTAL INFORMATION

The following schedules provide further detail, by major program area, of assets, liabilities and U.S. government equity; of revenue, financing sources and expenses; of sources and uses of funds by major program area and of budgeted and actual outlays.

- The medical program area includes financial data for the medical care program, including the VA's 172 medical centers, medical research and administration, and construction. The construction program was included since most of its activities relate to medical facilities.
- The veterans' benefits area includes the compensation, pensions and education programs, as well as the burial and miscellaneous assistance and veterans' job training programs.
- Housing credit assistance includes both VA's loan guaranty and direct loan programs.

- The administration area includes costs of managing the Agency as a whole and the National Cemetery System. Also included are costs of managing the Supply Fund and automated data processing systems.

Personnel compensation and fringe benefits for employees involved in veterans benefits, housing credit assistance and life insurance have not been allocated to these major program areas and are included in the administration area.

NOTE 10: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF ASSETS, LIABILITIES AND EQUITY BY MAJOR PROGRAM
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986

(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
ASSETS:						
Fund Balance with U. S. Treasury	$ 1,532,060	$ 1,917,862	$ 368,897	$ 24,817	$ 104,787	$ 6,148,601
Imprest Funds	9,790					9,790
Advances, Accounts, and Loans Receivable	215,204	414,697	1,208,749	1,695,768	69,947	3,606,365
Investments	19,671		134,800	11,635,018		11,789,489
Foreclosed Property Held for Sale			807,531			807,531
Land, Buildings, and Equipment Net of Accumulated Depreciation	6,307,381				2,668	6,310,049
Other Assets	14,544				120,041	156,585
Future Financing Sources	492,726		1,525,122		41,264	2,180,112
TOTAL ASSETS	$10,511,376	$ 2,332,559	$4,145,299	$13,355,603	$ 338,707	$30,784,525
LIABILITIES AND EQUITY:						
Accounts Payable, Principally to the Public	$ 612,829	$ 5	$ 109,371	$ 178,058	$ 141,645	$ 1,041,710
Accrued Compensation and Pension Benefits		1,253,671				1,259,671
Accrued Payroll and Payroll Related Liabilities	776,662				70,250	846,912
Dividends on Credit or Deposit				630,181		630,181
Insurance Dividends Payable				929,714		929,714
Other Liabilities	8,309	6,552	159,767	135,879	71,879	382,386
Reserve for Losses on Guaranteed Loans			1,735,252	0		1,735,252
Insurance Reserves				11,229,292		11,229,292
Borrowings from Treasury			1,730,078			1,730,078
TOTAL LIABILITIES	1,397,800	1,260,228	3,734,470	13,103,324	283,574	19,785,396
EQUITY OF THE U. S. GOVERNMENT:						
Unrealized Appropriations:						
Deferred Appropriations	6,337,930	107,222			167,783	6,612,935
Unobligated Balances	1,419,041	307,617	411,829		7,839	2,146,141
Undelivered Orders	1,435,594	3,151	1		79,511	1,518,269
Trust Fund Balances	21,011	648,491				669,502
Insurance Fund Balances				52,279		52,279
TOTAL EQUITY OF THE U. S. GOVERNMENT	9,213,576	1,066,311	411,829	52,279	255,133	10,999,128
TOTAL LIABILITIES AND EQUITY	$10,611,376	$ 2,332,539	$4,145,299	$13,155,603	$ 538,707	$30,784,524

NOTE 10: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF SOURCES AND USES OF RESOURCES AND RECONCILIATION TO BUDGET BY AGENCY PROGRAM
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986
(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
NET USE OF RESOURCES:						
Operations:						
Operating Expenses	$ 9,708,176	$ 15,695,819	$ 1,094,250	$ 1,112,457	$ 769,375	$ 28,380,275
Items Requiring (Providing) Funds:						
Increase in Insurance and Guaranteed Loan Reserves			(513,875)	(181,221)		(695,096)
Depreciation	(337,997)					(337,997)
Increase (Decrease)in Accounts Receivable	75,482	(35,798)	(5,633)	3,825	22,548	60,424
Decrease (Increase) in Accounts Payable and Accruals	(111,938)	1,592	(8,055)	(61,040)	5,276	(174,165)
Revenues Accounted for as Offsetting Collections	(258,716)	(298,682)	(441,848)	(1,067,561)	(46,505)	(2,114,310)
Funds Used (Provided) by Operations	9,076,005	15,362,930	(25,061)	(193,340)	750,692	25,119,328
Non-Operating Uses:						
Dividends				925,165		925,165
Acquisitions of Land, Buildings and Equipment	952,690					952,690
Purchase of Foreclosed Property Held for Sale			1,147,210			1,147,210
Issuance and Repurchase of Loans and Liens			969,590	119,491		1,089,081
Other, Net	4,065	7,531	24,487			36,083
Financing Activities:						
Sale of Foreclosed Property Held for Sale			(1,214,867)			(1,214,867)
Sale of Loans, with Recourse			(818,368)			(818,368)
Loan and Lien Repayments			(100,993)	(181,816)		(282,809)
Disposals of Equipment and Other	(145,328)	(96,812)		(54,396)		(296,536)
Revenues Collected for Treasury	(660)	(112,791)				(113,451)
NET USE OF RESOURCES (BUDGETARY OUTLAYS)	9,886,872	15,156,858	(24,100)	605,990	750,692	26,375,310
RESOURCES PROVIDED:						
Intra-agency Transfers	(43,984)	35,000			8,984	0
Current Year Appropriation	10,165,065	15,169,800	200,000	9,750	719,831	26,464,626
Less: Reductions Pursuant to P.L.99-177 (Gramm-Rudman-Hollings)	(156,659)	(45,232)		(5)	(32,577)	(234,053)
Current Year Appropriations, Net	9,966,402	15,339,568	200,000	9,745	716,658	26,230,373
Interest on Government Securities				963,956		963,956
Net Transfers, Reimbursements and Other	4,507	(107,428)	(2,120)	3,485	6,571	(95,185)
Funds Returned to Treasury	(53,151)	(785)			(4,787)	(58,723)
TOTAL RESOURCES PROVIDED	9,915,758	15,231,355	197,880	977,186	718,442	27,040,621
INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS	30,786	74,299	63,780	368,096	(32,250)	484,711
Funds Exchanged for U.S. Government Securities	(2,394)			(358,217)		(360,611)
NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS	28,392	74,299	63,780	(10,121)	(32,250)	124,100
U.S. TREASURY AND IMPREST FUNDS:						
Beginning of Year	3,513,458	1,843,563	305,117	34,938	337,817	6,034,893
End of Year	$ 3,541,850	$ 1,917,862	$ 368,897	$ 24,817	$ 306,567	$ 6,158,993

NOTE 10: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF EXPENSES, DIVIDENDS, REVENUE, AND FINANCING SOURCES BY MAJOR PROGRAM FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986

(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
OPERATING EXPENSES AND DIVIDENDS:						
Expenses By Category:						
Personnel Compensation and Fringe Benefits	$ 6,039,907				$ 542,565	$ 6,582,472
Veterans' Benefits		$ 15,695,819				15,695,819
Insurance Claims & Indemnities				$1,112,657		1,112,657
Depreciation	137,997					137,997
Supplies & Materials	1,525,631				12,140	1,537,771
Contractual Services	1,133,073				47,335	1,180,408
Rent, Communications and Utilities	374,624				128,822	503,446
Other	296,562		$1,044,250		88,513	1,429,325
Total Operating Expenses	9,708,174	15,695,819	1,095,250	1,112,657	769,375	28,380,275
Dividends to Policy Holders				938,251		938,251
	$ 9,708,174	$ 15,695,819	$1,095,250	$2,050,908	$ 769,375	$29,088,526
OPERATING REVENUE AND FINANCING SOURCES:						
Operating Revenues:						
Premium Income				$845,559		845,559
Interest Income			184,433	1,165,958		1,350,391
Loan Origination Fees			258,111			258,111
Reimbursements and Other	259,716	71,619	(698)		46,505	377,142
Total Operating Revenue	259,716	71,619	441,846	2,011,517	46,505	2,831,203
Financing by Source:						
Appropriations Realized	9,448,458	15,397,137	652,404	9,391	722,870	26,230,260
Transfers, Reimbursements and Other		227,063				227,063
Total Budgetary Financing	9,448,458	15,624,200	652,404	9,391	722,870	26,457,323
	$ 9,708,174	$ 15,695,819	$1,094,250	$2,020,908	$ 769,375	$29,288,526

NOTE 10: (CONTINUED) VETERANS ADMINISTRATION

BUDGETED AND ACTUAL OUTLAYS BY FUNCTION AND PROGRAM
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986

	Budgeted Outlays		
	President's Budget	Enacted * Bill	Actual Outlays
	(Dollars in Thousands)		
HOSPITAL AND MEDICAL CARE:			
Medical Care	$ 9,051,700	$ 9,067,560	$ 9,095,306
Medical and Prosthetic Research	187,080	181,491	181,246
Medical Administration	57,379	55,631	64,780
Construction	737,800	555,081	522,386
All Other	(27,192)	19,450	31,254
Total Hospital and Medical Care	10,006,767	9,879,213	9,884,972
BENEFITS:			
Income Security for Veterans:			
Compensation	10,194,000	10,453,000	10,416,201
Pensions	3,833,000	3,835,000	3,874,368
Burial and Other Benefits	136,800	128,007	121,909
Proposed Legislation	285,700		
Reinstated Entitlement for Survivors		14,970	9,856
Subtotal Income Security	14,449,500	14,430,977	14,422,334
Education, Training and Rehabilitation:			
Readjustment Benefits (G.I. Bill)	1,034,500	910,422	918,056
Post-Vietnam Era Education	40,000	(210,600)	(98,624)
Veterans Job Training	35,000	49,200	34,192
All Other	(7,570)	(158,215)	(119,102)
Subtotal Education, Training and Rehabilitation	1,101,930	590,807	734,522
Total Benefits	15,551,430	15,021,784	15,156,856
HOUSING CREDIT ASSISTANCE:			
Loan Guaranty	383,500	285,450	162,769
Proposed Legislation	(604,800)		
Direct Loans	(45,600)	(44,740)	(28,669)
Total Housing Credit Assistance	(266,700)	240,710	134,100
INSURANCE PROGRAMS	685,961	678,633	609,090
ADMINISTRATION	751,456	718,025	750,692
TOTAL	$26,728,914	$26,538,365	$26,535,710

*After reduction pursuant to P.L. 99-177 (Gramm-Rudman-Hollings). Where actual outlays exceeded outlays budgeted in the enacted bill, funds were obtained from available unobligated balances. This does not constitute a violation of the Anti-Deficiency Act (31 U.S.C. 1341).

STATEMENT OF

BOB MORAN, ASSOCIATE LEGISLATIVE DIRECTOR

PARALYZED VETERANS OF AMERICA

BEFORE THE

SUBCOMMITTEE ON COMPENSATION, PENSION AND INSURANCE

OF THE

HOUSE COMMITTEE ON VETERANS' AFFAIRS

CONCERNING

VA INSURANCE PROGRAMS

SEPTEMBER 10, 1987

Mr. Chairman and Members of the Subcommittee, on behalf of the members of Paralyzed Veterans of America, I wish to thank you for the opportunity to present the views and concerns of PVA regarding Veterans Administration insurance programs. I am Bob Moran, PVA Associate Legislative Director.

Our testimony will be limited to two of the insurance programs administered by the VA which directly affect PVA's members. They are National Service Life Insurance (RH Insurance) for veterans with service-connected disabilities and Veterans Mortgage Life Insurance for those veterans who have received a specially adapted housing grant.

The insurance programs administered by the Veterans Administration have long served as a necessary resource for many veterans (particularly severely disabled veterans) who otherwise would not have access to commercial insurance. The maximum levels for some VA insurance programs have not kept up with inflation, and their efficacy has substantially been reduced. For veterans to be well-served by these programs, VA insurance coverage must reflect the prevailing economic conditions of the nation: they need to be increased to levels comparable to those available through commercial insurance providers.

National Service Life Insurance (NSLI)

RH Insurance

RH insurance is a special type of National Service Life Insurance, which is available to veterans with service-connected disabilities. Any service-connected veteran released from active duty, on or after April 25, 1951, under other than dishonorable conditions is eligible to apply for this insurance. Good health, except for the service-connected disability, is a requirement. RH insurance is issued in amounts from $1,000 to $10,000, in multiples of $500, and the veteran cannot purchase any other insurance under any other federal government life insurance program, which would total more than $10,000.

PVA's concern is with the low amount of insurance coverage provided under this type of policy. It must be kept in mind that it is this same service-connected disability that hinders the veteran from purchasing insurance from commercial companies at a reasonable premium.

Commercial insurance companies estimate the appropriate amount of insurance protection required by an individual by using the factors of age, life expectancy, number of dependents and annual earning capacity. By using these factors, the dollar value of insurance necessary to provide for adequate protection is derived. The maximum amount of NSLI, $10,000, is not sufficient to meet today's obligations when compared to the recommendation of private insurers.

For a spinal cord injured veteran, using the criteria established by private insurers, adequate coverage should be over $150,000. This is based on a veteran aged 44, married with two children, average life expectancy of 70, with a monthly compensation of approximately $2,100. The appropriate amount of coverage is developed by using the insurance industry's formula of taking the annual income and multiplying by a factor of six. For the above veteran using this formula, the total family protection the veteran should carry is $151,200.

It is apparent that a policy (NSLI) designed over 30 years ago is inadequate today. It has not been increased to offset rising economic factors, and it

does not permit the catastrophically disabled veteran the opportunity of providing long-term financial security. PVA strongly recommends that the Subcommittee consider raising the NSLI RH insurance from the maximum of $10,000 to $50,000. Also, have a one year open enrollment period to allow eligible veterans the opportunity to purchase additional amounts of RH insurance in increments of $10,000, up to an additional $100,000.

With the $50,000 insurance offered by the VA, and with the veteran having the option of purchasing additional amounts of insurance ($100,000 maximum), it would give a more realistic insurance coverage of $150,000, more in keeping with the adequate coverage recommended by commercial insurance companies. These alternatives would add minimal administrative costs to the V.A., yet, allow those veterans who need more protection the opportunity to provide needed security for their families.

Veterans Mortgage Life Insurance (VMLI)

Another concern of PVA is the Veterans Mortgage Life Insurance Program. This type of insurance became available on August 11, 1971, with the enactment of Public Law 92-95. VMLI is a program of group-type mortgage life insurance for service-connected disabled veterans who have been granted a specially adapted housing grant under Chapter 21, Section 801 of Title 38 USC.

VMLI provides mortgage insurance for severely disabled veterans who would not otherwise be able to obtain coverage because of their medical conditions. The present maximum coverage was increased to $40,000 through provision of Public Law 94-433, effective October 1, 1976. Protection is automatic for the amount of the mortgage, up to the maximum of $40,000, unless eligible veterans decline in writing or fail to respond to a final request for information on which their premium can be based.

Premiums are automatically deducted from any compensation or other cash benefits payable to them by the VA. Any veteran insured, not eligible for cash benefits from the VA, may pay the amount of his premiums directly to the insurer. The policy remains in effect until the mortgage, up to the maximum $40,000 has been liquidated, or the home is sold; or until the veteran reaches 70 years of age, or dies. If a mortgage is disposed of through

liquidation or sale of the property, any unused portion of the mortgage life insurance policy may be used on the mortgage of a subsequent home.

VMLI is made available to assist the following veterans entitled to compensation for permanent and total service-connected disability:

1) due to the loss, or loss of use, of both lower extremities, such as to preclude locomotion without the aid of braces, crutches, canes, or a wheelchair, or

2) which includes (A) blindness in both eyes, having only light perception, plus (B) loss, or loss of use of one lower extremity, or

3) due to the loss, or loss of use, of one lower extremity together with (A) residuals of organic disease or injury, or (B) the loss, or loss of use of one upper extremity, which so affect the functions of balance or propulsion as to preclude locomotion without the aid of braces, crutches, canes, or a wheelchair.

This strict criteria for veterans to obtain VMLI limits the eligibility to a relatively small number of veterans, consequently, the cost to the government is not great.

Mr. Chairman, PVA believes the cost factors involved in new home construction are well known to all Members of the Subcommittee. A brief summary of the escalating cost of housing, including the VA amounts for the Grant and VMLI are as follows:

Year	Housing Costs	VA Grant	VMLI
1976	$57,789 *	$25,000	$40,000
1986	$111,900 *	$35,500	$40,000

*Source-National Home Builders (national average).

Mr. Chairman, while the figures themselves provide evidence of the escalating cost of housing (in 10 years housing costs have nearly doubled), it is clear

that VMLI is not keeping pace with today's economic situation. The following illustration shows that a veteran who buys a specially adapted house, utilizing the maximum amount of the VA grant and the maximum amount of VMLI, cannot be assured of providing mortgage-free housing for his spouse and dependents upon his death.

Today's Average Housing Cost	$111,900.00
VA Grant	$35,500.00
Total Mortgage	$76,400.00
VMLI Protection	$40,000.00
Unprotected Mortgage Remaining	$36,400.00

PVA advocates that VMLI maximum coverage be increased to $70,000 to more accurately reflect the increased amount of mortgage which is likely to remain after the veteran's death. PVA continues to receive correspondence from widows who are forced to sell the family home when faced with a high mortgage, increased taxes, and a drastically lower Dependency and Indemnity Compensation payment upon the death of the veteran.

Veterans Eligible for NSLI RH Insurance and VMLI

There are certain veterans that due to their service-connected disabilities, (the more catastrophically disabled) that are eligible for both NSLI RH Insurance and VMLI. Under existing law, veterans may not buy any amount which, added to any Government Life Insurance they currently have, that would total more than $10,000.

A change in current law or a provision applying only to those veterans who fall under this category should be considered. One possible suggestion would be a cap or maximum amount not to exceed $150,000 between any two combinations of insurance from NSLI RH Insurance and VMLI. It must be remembered that this particular group of veterans, due to their service-connected disabilities, are restricted in purchasing commercial insurance.

Conclusion

Mr. Chairman, in conclusion, I wish to reiterate PVA's concerns. First, we believe that NSLI RH insurance should be increased by the alternative PVA has suggested to reflect the current requirements for providing adequately for a veteran's survivors. PVA recommends raising the amount of NSLI RH insurance and providing the veteran the opportunity to purchase additional amounts of insurance coverage. Secondly, VMLI should be increased from $40,000 to $70,000, to reflect the rising cost of housing and allow our nation's severely disabled veterans sufficient coverage to provide adequately for their families.

Mr Chairman, I want to extend PVA's appreciation to you and members of the Subcommittee for your ongoing efforts to improve the effectiveness of these most important programs that directly affect our members and their dependents, and for allowing PVA to testify and work with you and your professional staff in this endeavor. This concludes my testimony, and I will be glad to answer any questions that I can.

STATEMENT OF

GORDON R. THORSON, SPECIAL ASSISTANT
NATIONAL LEGISLATIVE SERVICE
VETERANS OF FOREIGN WARS OF THE UNITED STATES

BEFORE THE

SUBCOMMITTEE ON COMPENSATION, PENSION AND INSURANCE
OF THE
COMMITTEE ON VETERANS' AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

WITH RESPECT TO

THE CURRENT STATUS OF VETERANS ADMINISTRATION INSURANCE PROGRAMS

WASHINGTON, D. C. SEPTEMBER 10, 1987

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

Thank you for inviting the Veterans of Foreign Wars of the United States to participate in this important hearing. I am privileged to represent the opinion of our proud organization and consider it an honor to appear before this congressional Subcommittee. The VFW and its Ladies Auxiliary are comprised of 2.8 million men and women and many of our members participate in VA insurance programs. The low-cost family protection afforded to veteran participants by the existing insurance programs are for the most part very well conceived and considered valuable.

The hearing today is convened to discuss the current status of the various insurance programs. We compliment the Chairman for scheduling this hearing and offering our organization an opportunity to participate in the oversight process. The Subcommittee should be further commended for its continued efforts to monitor and steadily improve the VA insurance program thus contributing substantially to its continued success. The VFW certainly appreciates this opportunity to discuss and offer suggestions that could further enhance the insurance program.

In preparation for today's testimony we contacted VFW Department Service Officers (DSOs) who have direct contact with the VA Insurance Centers in St. Paul, Minnesota (Fort Snelling) and in Philadelphia, Pennsylvania. Our DSOs give a glowing report on activities at both insurance centers. In fact, it should be noted that every courtesy and full cooperation are extended to our DSOs by all insurance center personnel. This reflects well on the staff and the leadership of both centers.

Though the VFW is highly complimentary of the VA Insurance Center, programs and staffing, we do, however, have a few suggestions that could further improve the program. The Veterans Administration Central Office continues to push for consolidation of the insurance office at Fort Snelling with the office in Philadelphia. The VA Administrator asserts that this move would save money and improve operational efficiency. Mr. Chairman, the Veterans of Foreign Wars does not, will not and cannot support or agree with any effort to eliminate the VA Insurance Center at Fort Snelling in St. Paul, Minnesota. The delegates to the 88th National Convention of the Veterans of Foreign Wars of the United States met in New Orleans, Louisiana from August 14 through 21 and passed a resolution that specifically calls for the retention of the VA Insurance Center in St. Paul, Minnesota. Attached to this written testimony is a copy of Resolution Number 730, titled "Retention of VA Regional Insurance Center at St. Paul, Minnesota." Resolution Number 730 further makes the case for utilizing Building 43 at the VA Medical Center in Minneapolis as a new home for the insurance activity.

The VFW would like to go on record thanking Congressman Timothy J. Penny for his considerable efforts directed at protecting the St. Paul facility from elimination. Congressman Penny with the support of the House Veterans' Affairs Committee and others have advanced legislation, a

provision within H.R. 2945, that would once and for all prevent the VA from closing the St. Paul VA Insurance Center and consolidating its insurance activities in Philadelphia. The full House has approved and supports retention of the St. Paul facility and we see no reason why the Senate should not follow suit.

Secondly, the VFW would like to direct the Committee's attention to mortgage insurance for certain disabled veterans. Too often veterans suffering from a service-connected disability, and who are not entitled to special adapted housing allowance, cannot obtain mortgage protection life insurance other than high risk insurance which carry very high premium rates. All too often these rates are beyond the veterans financial capability. We would support the introduction and passage of legislation that would provide affordable mortgage insurance to this special group of veterans, thus allowing them an opportunity to provide their families with the security of a mortgage free home if they should die.

We have one further suggestion that could improve the "RH" Insurance program and better serve the service-connected veteran. The letters "RH" identifies certain National Service Life Insurance policies that have been issued since April 25, 1951, to veterans with service-connected disabilities. This is the only insurance currently being issued by the Veterans Administration. Application must be made within one year from the date of notification by the VA that a disability is service connected. Normally, the VA notifies the veteran of his service-connected status by mailing him an "Award Letter." The date shown on this notice is the date used to establish the one year eligibility period. Now, here is the problem. VA Regional Office's (VARO) periodically send listings of eligible veterans to the appropriate insurance division, the insurance division then in turn notifies the veteran of his eligibility for "RH" National Service Life Insurance; oftentimes, however the VA Regional Offices delay notifying the Insurance Division in a timely fashion and some VAROs forget to even forward the name of eligibles. As a result veterans are sometimes not given adequate time to make an educated decision on this valuable insurance and sometimes eligible veterans aren't even notified of their eligibility. This is unacceptable to the VFW and we suggest that some changes need to be made.

We suggest that an effort be made to ensure that veterans are notified immediately of their eligibility for "RH" National Service Life Insurance. This could be best accomplished by the originating VA Regional Office. A mechanism could be put in place to automatically trigger an insurance eligibility letter when the regional office generates the service-connected award letter. This action would give the eligible veteran the full one year grace period as provided under law to make this important decision.

In closing the VFW would again like to thank this Subcommittee. This concludes my statement. Thank you.

The American Legion
For God and Country

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September 11, 1987

Honorable Douglas Applegate
Chairman
Subcommittee on Compensation, Pension
and Insurance
House Committee on Veterans Affairs
335 Cannon House Office Bldg.
Washington, DC 20515

Dear Mr. Chairman:

The American Legion is appreciative of the opportunity afforded us to present for the hearing record our views on the insurance programs presently available to present and former service members of the Armed Forces of the United States. In doing so we would point out that our Organization is the only service organization to our knowledge that maintains a full insurance service, with personnel assigned to both the Philadelphia and St. Paul Insurance Centers. We believe this gives us a special ability to evaluate and comment on the VA's insurance programs.

Insurance programs presently being administered by the Veterans Administration are divided between those administered directly by the VA for veterans who served through the 1950's, the United States Government (USGLI) and the National Service (NSLI) Life Insurance programs, and the Servicemen's Group (SGLI) and Veterans Group (VGLI) Life Insurance programs begun in 1965 for those in active and reserve service, and those in active reserve and ending service statuses respectively, which are supervised by the VA but administered by the Prudential Insurance Company of America in Newark, New Jersey.

With regard to the overall performance of the programs, it appears to us this has been generally adequate. However, the USGLI and NSLI programs have suffered from budget cuts, from the downgrading of employee salary positions at the operative level (with resultant turnover), and from the retirement of many highly

experienced personnel. VA is continuing a process, begun years ago, to automate their in-house systems with new online direct mainframe input and output ADP systems to offset these effects and provide an ever increasing level of service to insured veterans. At present funding is adequate for this insurance redesign effort and The American Legion urges that it be maintained and given full support by Congress to ensure that veterans and their beneficiaries receive prompt service from a responsive agency. It should go without saying that insurance is one of the most important factors in the lives of families - especially during times of personal crisis.

One other important problem we have encountered in the USGLI and NSLI programs lies in the timely processing of insurance payments of various kinds to recently deceased veterans, which then must be cancelled and reissued to their designated beneficiary. Associated with this is the unending task of tracing lost payments for appropriate action. Both of these are basically in the area of responsibility of the Treasury Department. VA maintains a continuing dialogue with Treasury to achieve problem resolution, but has been hampered in delivery of service to insureds and beneficiaries by the Treasury making unilateral decisions in the method of service, data format and data delivery systems they provide, which have often not coincided with VA systems and needs. This, plus the Treasury's priorities in servicing other Federal agencies such as Social Security and the IRS, have resulted in continuing delays in the processing of insurance payments; delays often exceeding eight to ten weeks in duration, with resulting real hardship to veterans and their families. The American Legion supports the VA in this matter. We believe the Treasury Department should be required to give greater emphasis to providing service to veterans and their beneficiaries, especially in view of the fact the benefits sought have been bought and paid for by the veterans.

Delays of another type continue to be experienced by active duty and reserve personnel who are covered by the SGLI program. When a service person dies while on active duty (and/or reserve active duty), as some two thousand do annually, even now in peacetime, there are often delays of weeks and months in getting their servicemen's life insurance payments delivered to their beneficiaries - who are oftentimes in great financial need (this insurance benefit was increased to a maximum of $50,000 in October 1985). The reason for such delay is that the program administrator, Prudential Insurance, does not maintain coverage records itself and relies on the military service departments to provide necessary information on SGLI status, including the amount held, and the beneficiary. This entails waiting for receipt of the needed information from personnel centers of the military departments, or from the St. Louis Reserve Center. The resolution of this problem, in our judgment, lies in further DOD

automation of service personnel 201 and emergency (e.g., NOK) data files, so that SGLI coverage and beneficiary information is included on a continually updated basis, and for this to be appropriately linked with the Prudential center for timely payment of claims. Considering the circumstances in which many of our service personnel are now required to serve, with increased risk, we believe these improvements take on added importance.

On the positive side the VA continues to provide the maximum insurance benefits it can, under existing law, to current and prior military personnel. As mentioned earlier the death benefit under the SGLI and VGLI programs was raised to an optional ceiling of $50,000 in October 1985. The amount of additional paid-up insurance, obtainable by election through use of annual policy dividends, for those veterans insured under the NSLI program was increased from its base level 15% effective January 1, 1987, to allow greater coverage build up over time for their beneficiaries. Many policies are now seeing such balances exceed the NSLI maximum face value of $10,000, thereby effectively doubling the amount of coverage held. Finally, interest charged on insurance policy loans for those insureds with permanent plan NSLI policies is being annually adjusted to float with certain long term treasury security market rates. This allows more equitable distribution of the return of NSLI trust fund investments (dividends) between those who borrow against their life insurance policies and those who do not.

Let us turn now to a measure being proposed to Congress by VA for appropriate legislation.

The first proposal deals with NSLI and its "V" policies, and relates to the amount of monthly installments, when insurance proceeds are paid out as an annuity rather than in a one sum, and current legal limitations requiring, as per Sections 702, 723, 725 and 744 of title 38, USC, the use of specific interest rates, rather than broad factor increases, in the calculation of annuity amounts. VA advises, given present funds earnings and mortality experience, gains from the annuity settlement reserves themselves are now over $37 million a year, with projections by their actuaries showing such to remain at some $33 million annually through 1989. These gains should, of course, be paid to the annuitants, many of whom are elderly and very needy, and not simply put back into the general reserve (as is now required) for payments as increased dividends to living insureds; it is the annuitants reserves which are generating the aforementioned gains. Increasing the annuity calculation interest rates (ref. 38 USC 726 and 761) would not accomplish a fair distribution. Rather, general increases of payments by fixed percentages would, and the VA desires such an increase on the NSLI "V" policies (the only policies whose performance justifies such action, but the

largest of the program categories) by some 50% at least, for the next five years. Such adjustments entail no relevant savings or costs to the Government above current levels and are wholly fair. The American Legion believes the appropriate legislation, H.R. 2008, should be enacted.

The second measure involves the SGLI and VGLI programs, and the changing of 38 USC 769 to forbid by law the taxing in any way of premiums of such insurance by any political entity of the United States. More than $46 million has been taken in taxes on the payments of premiums for both programs since their beginning in 1965. Not only in taxes, but in licenses and fees as well, all levied by the States and other taxing authorities such as Puerto Rico and the District of Columbia. Naturally, the higher the expenses of the programs the higher the premiums charged to active and reserve duty personnel, and to veterans. In addition, besides the extraordinary nature of the users of these insurance services - the men and women who are and have served in uniform - we find even ordinary civilian employees of the Federal Government were so exempted in their premium taxes under the Federal Employees Group Life Insurance Program in 1980, by Public Law 96-499. Surely those who do and have served in our military services deserve no less, and The American Legion urges the proposed legislation (H.R. 2008 also) be enacted as soon as possible.

In conclusion, Mr. Chairman, we believe it is fair to say that the life insurance programs offered by the Government to service members and veterans is often the single most important thing that can be done for them in recognition of their service. The American Legion supports wholeheartedly the efforts of the Veterans Administration to improve its service in this program area, and we also appreciate the interest and concern of the Subcommittee, and of the entire Committee, in responding to the problem areas we have discussed herein.

Sincerely,

E. PHILIP RIGGIN, Director
National Legislative Commission

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October 2, 1987

Honorable Thomas K. Turnage
Administrator of Veterans Affairs
Veterans Administration
Washington, DC 20420

Dear General Turnage:

In reference to our Compensation, Pension and Insurance hearing of September 10, 1987, I would appreciate it if you could answer the enclosed questions submitted by Representative Bob McEwen, by October 26, 1987.

In an effort to reduce printing costs, the Committee on Veterans' Affairs, in cooperation with the Joint Committee on Printing, is implementing some formatting changes for materials for all full Committee and Subcommittee hearings. Therefore, it would be appreciated if you could provide your answers consecutively on legal size paper, single spaced.

Sincerely,

G. V. (SONNY) MONTGOMERY
Chairman

GVM:das

Enclosure

cc: R. J. Vogel

Office of the
Administrator
of Veterans Affairs

Washington DC 20420

Veterans
Administration

OCT 30 1987

Honorable G. V. (Sonny) Montgomery
Chairman, Committee on Veterans'
Affairs
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Enclosed please find answers to the questions raised by Representative Bob McEwen following the Subcommittee on Compensation, Pension and Insurance's hearing of September 10, 1987, on VA Insurance Programs. I appreciate the opportunity to provide this additional information for the record.

Sincerely,

THOMAS K. TURNAGE
Administrator

Enclosure

cc: Representative Bob McEwen

QUESTIONS OF CONGRESSMAN BOB MCEWEN OF OHIO
TO THE VETERANS ADMINISTRATION
SUBCOMMITTEE ON COMPENSATION, PENSION AND INSURANCE

HEARING OF SEPTEMBER 10, 1987

Question 1: The estimated unfunded liability of $629 million in the Service-Disabled Veterans Insurance program represents a pay out over what period of time?

Answer 1: The estimated unfunded liability of $629 million (as of September 30, 1986) in the Service-Disabled Veterans Insurance (S-DVI) program represents the sum of all future benefits not covered by premiums. The $629 million represents a pay out of approximately 82 years. This is calculated by deducting the youngest age of a S-DVI policyholder (18) from the maximum policy maturity age (100).

Question 2: How are current interest rates on NSLI policy loans determined, and what is the current rate?

Answer 2: The current NSLI policy loan interest rate is an 11 percent fixed rate. A new variable loan rate is being implemented on November 2, 1987 and will be set initially at 8 percent. The regulatory amendment which authorizes the rate reduction provides for annual adjustments to the policy loan interest rate. Each year the VA will make a determination as to whether a rate adjustment is needed by monitoring the Ten-Year Constant Maturities Index for U.S Treasury Securities, for the month of June. If an adjustment is necessary, it will be made effective on the following October 1st. Policyholders with existing variable rate loans will be notified in advance of any rate increases. Notice of any rate changes will also be published in the Federal Register.

If an adjustment is made, the new rate will equal the June level of the economic indicator rounded down to the next whole number, unless this would cause the rate to be lower than 5 percent or exceed 12 percent. In that event, the rate will be set at the closest whole percentage within the permitted range - either 5 or 12 percent.

Shortly after the regulatory amendment becomes effective, we plan to take action which will benefit approximately 80,000 policyholders with NSLI loans at the 11 percent fixed rate. These policyholders will be provided a special opportunity to exchange their 11 percent loans for variable rate loans at 8 percent. We believe that the majority of these policyholders will recognize the advantages of this offer, and will switch to the variable rate.

Question 3: Why was the new interest rate regulation proposed?

Answer 3: The current fixed policy loan interest rate was increased from 5% to 11% in 1981. The decision to increase the interest rate in 1981 was based, in part, upon the widening gap that had developed between the earnings on trust funds invested in U.S. securities and the return on the funds diverted to policy loans. The 11% rate was set based on a formula which was tied to the yield on long-term Treasury securities.

With the general decline in interest rates in the economy, the VA initiated a change in the rate which reflects the current trend in long-term Treasury securities. A variable rate was adopted so that adjustments will be made on an annual basis.

QUESTIONS OF CONGRESSMAN BOB MCEWEN OF OHIO
TO THE VETERANS ADMINISTRATION
SUBCOMMITTEE ON COMPENSATION, PENSION AND INSURANCE

HEARING OF SEPTEMBER 10, 1987

Question 4: Is the VA doing a study on privatizing some of its life insurance programs. Please describe the study.

Answer 4: The three Government life insurance programs established after 1965 are already administered by private insurance companies through contractual agreements with VA. These are the Servicemen's Group Life Insurance (SGLI), the Veterans Group Life Insurance (VGLI) and the Veterans Mortgage Life Insurance (VMLI) programs.

No study of the privatization of the five programs currently administered by the VA is currently underway. A study was conducted by the Office of the Inspector General in 1984 which reviewed the costs of the VA administered programs in comparison to commercial insurance company costs. That study concluded, "Although the usefulness of available cost data for VA and private industry operations was restricted for detailed comparison because of different methods of classifications and computation of data, the resultant unit costs per policy reported by VA and industry are useful for overall comparison purposes. Our review indicates all significant VA costs are included in the $5.975 cost per policy and we accept the industry costs of $6.533 per group life policy and $50.486 per ordinary life policy. We believe they support the current in-house delivery method for the five VA administered programs."

Question 5: How much is VA spending to redesign and upgrade the automated data processing system which supports the insurance program?

Answer 5: The estimated cost to redesign and upgrade the automated data processing system which supports the Insurance program is $2,993,000 in FY 1987, $4,423,000 FY 1988 and $3,239,000 in FY 1989. This includes all major in-house development and contract expenditures for hardware and software including the cost associated with conversion of the Insurance program from the antiquated Autocoder language to ANSI COBOL. These figures represent gross costs which do not reflect the savings to be realized once the redesigned system is fully installed.

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